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Supreme Court of the United States

WILLIAM J. BROWN, JR. AND MORRIS AND  
OAKLAND TRUST CO. BY GERALD F. GULKIN,  
THAT THEY BE REVERSED, APPELLANTS.

CITY BANK SAVINGS & TRUST COMPANY, AS  
TRUSTEE OF THE WILL OF HENRY C.  
WILLIAMS, DECEASED, RESPONDENTS.

Appeal from the Appellate Division, New York County,  
City of New York.

THOMAS M. BROWN

# SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1943

No. 52

WILLIAM J. DEMOREST, JR., ANN DEMOREST AND  
CAROLYN DEMOREST BY GERALD P. CULKIN,  
THEIR SPECIAL GUARDIAN, APPELLANTS,

vs.

CITY BANK FARMERS TRUST COMPANY, AS  
TRUSTEE UNDER THE WILL OF HENRY C.  
WEST, DECEASED, ET AL.

APPEAL FROM THE SURROGATE'S COURT, NEW YORK COUNTY,  
STATE OF NEW YORK

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**IN SURROGATE'S COURT, COUNTY OF NEW YORK**

File No. P1379—1934

In the Matter of the Judicial Settlement of the Account of Proceedings of CITY BANK FARMERS TRUST COMPANY as Trustee of the trusts created under the Last Will and Testament of HENRY C. WEST, Deceased, and of Application of CITY BANK FARMERS TRUST COMPANY as Trustee as aforesaid, for a Determination as to the Construction and Effect of said testator's Last Will and Testament, and for Instructions and Directions as to the Manner and Method of Allocation and Distribution of the Funds which are now or may hereafter be in its hands as Trustee as aforesaid.

NOTICE OF APPEAL OF INFANT APPELLANTS, WILLIAM J. DEMOREST, JR., ANN DEMOREST AND CAROLYN DEMOREST

SIRS:

Please take notice that Gerald P. Culkin, as Special Guardian for William J. Demorest, Jr., Ann Demorest and Carolyn Demorest; respondent in the above-entitled action, hereby appeals on the law and on the facts to the Appellate Division of the Supreme Court of the State of New York, First Department, from each and every one of the provisions of the decree in the within proceeding construing [fol. 5] the Will of the above-named deceased and settling the account of proceedings of City Bank Farmers Trust Company as Trustee of the trusts created under the Last Will and Testament of HENRY C. WEST, deceased, which decree was dated the 8th day of September, 1941, and made and entered herein in the office of the Clerk of this Court on the 9th day of September, 1941, and that said respondent, GERALD P. CULKIN, as Special Guardian as aforesaid, appeals from the whole and every part thereof except so much thereof as determines the true meaning and construction of the FIFTH clause of the Last Will and Testament of the above-named deceased and directs the disposition of the income from the trust created under said clause, to wit: paragraphs "1." to "4." thereof and except so much thereof as fixes the amount and directs the payment of costs, dis-

bursements, fees and allowances to counsel and special guardian.

AND PLEASE TAKE FURTHER NOTICE that the appellant having appealed upon the facts will request the Court to exercise its powers under section 309 of the Surrogate's Court Act.

Dated: New York, October 11th, 1941.

Yours, etc., GERALD P. CULKIN, *Special Guardian for Respondents William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, Infants*, Office and P. O. Address, 29 Broadway, Borough of Manhattan, City of New York.

[fols. 6-10] To MITCHELL, TAYLOR, CAPRON & MARSH, Esqs., *Attorneys for Petitioner*, 20 Exchange Place, New York City., LARKIN, RATHBONE & PERRY, Esqs., *Attorneys for Emma M. West*, 70 Broadway, New York City. BUTLER, WYCKOFF & REID, Esqs., *Attorneys for Marie Elizabeth West Jones and Elizabeth Francis Jones*, 165 Broadway, New York City. GEORGE LOESCH, Esq., *Clerk of the Surrogate's Court*, County of New York.

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[fol. 11] IN SURROGATE'S COURT, COUNTY OF NEW YORK

[Title Omitted]

DECREE CONSTRUING WILL AND SETTLING ACCOUNT—Sept. 8, 1941

City Bank Farmers Trust Company (formerly known as The Farmers' Loan and Trust Company) having heretofore on or about the 2nd day of December, 1940, filed an intermediate account of its proceedings as trustee under the last will and testament of Henry C. West, deceased, and [fol. 12] having also presented a petition praying that said account be judicially settled and allowed, that the court determine the construction and effect of the Fifth clause of said will as to whether after the death of Zimri West, Emma M. West is entitled to the entire income of the trust created pursuant to the said clause during her life or until she shall remarry, and that the court construe said will for the purpose of determining what proportion, if any, of the moneys or property received or which may be re-

ceived by way of rents or proceeds of sale of real property acquired upon foreclosure or by deed in lieu of foreclosure of mortgages or on account of claims based upon the guaranty of such mortgages, should be apportioned either to income or principal of the trust estate created by said will and what part, if any, may or should be paid or applied to the use of those persons who now or hereafter may be entitled to receive or have applied to their use the income of said trust estate, and that petitioner be instructed with respect to the proper method under the true construction of said will which should be employed in computing the net rents received from such or similar properties and the proper method of apportioning between principal and income such net rents, proceeds of sale of said properties or similar properties which may be hereafter acquired by said petitioner and of any moneys received or which might be received on account of any claims based upon such guaranties, and a citation having thereupon been duly issued, pursuant to statute directed to all the persons interested in the said trust created under said last will and testament of Henry C. West, deceased, citing and requiring them and [fol. 13] each of them to show cause before the Surrogate's Court of the County of New York, to be held at the Hall of Records, in the Borough of Manhattan, City, County and State of New York, on the 3rd day of January, 1941, at 10:30 o'clock in the forenoon of that day why said account should not be so judicially settled and allowed and said will should not be construed as prayed for in the petition and petitioner should not receive instructions as prayed for in said petition; and an order bearing date the 2nd day of December, 1940, having been duly made and entered herein on or about December 9, 1940, designating Gerald P. Culkin, Esq., counsellor-at-law, of 31 Nassau Street, City of New York, to receive service on behalf of William J. Demorest, Jr., and Ann Demorest, infants over the age of fourteen years, and Carolyn Demorest, an infant under the age of fourteen years; and the said citation having thereupon been returned with proof of due service thereof on Zimri West, 3rd, individually and as an heir-at-law and next-of-kin of Zimri West, deceased, Marie Elizabeth West Jones, individually and as an heir-at-law and next-of-kin of Zimri West, deceased, Elizabeth Frances Jones, Dilys Demorest, William J. Demorest, Jr., Ann Demorest, Carolyn Demo-

rest, Gerald P. Culkin, Esq., the person designated to receive service of the citation herein on behalf of William J. Demorest, Jr., and Ann Demorest, infants over the age of fourteen years, and Carolina Demorest, an infant under the age of fourteen years, and Emma M. West having appeared herein by her attorneys, Messrs. Larkin, Rathbone & Perry, pursuant to authorization duly acknowledged and filed herein, and Marie Elizabeth West Jones and Elizabeth Frances Jones having appeared herein by their attorneys, [fol. 14] Messrs. Butler, Wyckoff & Reid, pursuant to authorization duly acknowledged and filed herein, and said petitioner having duly appeared on the return day of said citation by Messrs. Mitchell, Taylor, Capron & Marsh, its attorneys, and said Emma M. West having duly appeared by her attorneys, Messrs. Larkin, Rathbone & Perry, and Marie Elizabeth West Jones and Elizabeth Frances Jones having duly appeared by their attorneys, Messrs. Butler, Wyckoff & Reid, and none of the other respondents herein having appeared, and Gerald P. Culkin, Esq., having been duly appointed special guardian for the infant respondents, William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, and having duly filed his consent to act herein, and City Bank Farmers Trust Company having duly rendered an account of its proceedings as trustee under the last will and testament of Henry C. West, deceased, to and including the 31st day of July, 1940, under oath before the said Surrogate and said account having been filed and said Gerald P. Culkin, Esq., having duly made and filed his report as special guardian herein duly verified on the 16th day of January, 1941, wherein objections numbered I to VI to said account were interposed, and said respondent, Emma M. West, by her attorneys, Messrs. Larkin, Rathbone & Perry, having made and filed objections numbered 1 to 15 to said account; and the matter having duly come on to be heard before the said Surrogate on the 17th day of January, 1941, and said petitioner, City Bank Farmers Trust Company, having duly appeared on said hearing by its attorneys, Messrs. Mitchell, Taylor, Capron & Marsh, C. Alexander Capron, Esq., and James K. Taylor, Esq., of counsel, the respondent, Emma M. West, having duly ap- [fol. 15] peared by her attorneys, Messrs. Larkin, Rathbone & Perry, Albert Stickney, Esq., of counsel, and the respondents, Marie Elizabeth West Jones and Elizabeth Frances Jones having duly appeared by their attorneys, Messrs.



Butler, Wyckoff & Reid, James Morrow, Esq., and also James L. Handford, Esq., of the New Jersey bar, of counsel, and the infant respondents, William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, having duly appeared by their special guardian, Gerald P. Culkin, Esq.; and the matter having been duly argued by counsel for the respective parties hereto and due deliberation having been had and the said Surrogate having rendered and filed his decision in writing herein, published in the New York Law Journal on the 3rd day of February, 1941, construing the Fifth clause of said last will and testament of Henry C. West, deceased, and determining the disposition of the income of the trust created under said last will and testament as hereinafter more particularly set forth;

And It Appearing that in and by said Fifth clause of his last will and testament, said Henry C. West, deceased, provided in part as follows:

"Fifth: All the rest, residue and remainder of my estate, \* \* \* I give, devise and bequeath to The Farmers' Loan and Trust Company \* \* \* In Trust Nevertheless, for the following uses and purposes: \* \* \* to apply the net income from said estate to the use of my wife, Emma M. West, during the term of her natural life, or until she shall remarry; Provided, However, that during the life of my said wife, Emma M. West, but not after her death, there shall be first ap- [fol. 16] plied out of the said net income the sum of One hundred dollars (\$100.) per month to the use of my brother, Zimri West. If my said wife shall remarry, the aforesaid payment to my said brother shall continue to be made as long as my said wife lives."

And It Further Appearing that Zimri West, brother of the decedent, mentioned in the hereinabove quoted provision of the last will and testament of said Henry C. West, deceased, died on or about the 15th day of February, 1940, a resident of the City of Maplewood, County of Essex, State of New Jersey, and that no legal representative of said Zimri West has been appointed and that Zimri West was survived by his son, the respondent, Zimri West, 3rd, and his daughter, the respondent, Marie Elizabeth West Jones, who are his heirs-at-law and next-of-kin, and that no other child or children of deceased children nor widow survived said Zimri West.

And It Further Appearing that the respondent, Emma M. West, mentioned in the hereinabove quoted provision of the last will and testament of said Henry C. West, deceased, is still living and has not remarried; it is

Ordered, Adjudged and Decreed, Found and Determined as follows:

1. That said testator, Henry C. West, deceased, intended to and did provide in and by the Fifth clause of his last will and testament, and the true meaning and construction thereof is, that the monthly payment of \$100 directed to be applied to the use of the testator's brother, Zimri West, [fol. 17] should be continued only during the life of his said brother, even though testator's wife, Emma M. West, should survive said brother;

2. That Emma M. West is now and has been since the 15th day of February, 1940, the date of the death of Zimri West, entitled to have the entire income from the trust, created under the Fifth clause of the last will and testament of Henry C. West, applied to her use during her life or until she shall remarry;

3. That the estate of Zimri West, deceased, is not and has not been entitled to any part of the income of said trust created under the Fifth clause of the last will and testament of Henry C. West, deceased, except such income as may have accrued to February 15, 1940, the date of the death of said Zimri West;

4. That neither Zimri West, 3rd and Marie Elizabeth West Jones who are now presumptively entitled to the income of the trust created under the Fifth clause of the last will and testament of Henry C. West, deceased, after the death or remarriage of Emma M. West, nor those who may hereafter be so presumptively entitled to the income of said trust from time to time hereafter, are entitled to have applied to their use any part of the income of said trust during the life of Emma M. West or until she shall remarry.

And the stipulation of all the parties who have appeared herein dated January 22, 1941, having been duly filed herein and the affidavit of James K. Taylor, Esq., duly sworn to on the 15th day of February, 1941, having been duly filed herein and the said Surrogate having rendered and filed his [fol. 18] decision in writing herein published in the New

York Law Journal on the 10th day of March, 1941, and said Gerald P. Culkin having duly made and filed his supplemental report herein duly verified the 27th day of March, 1941, wherein he reported said account to be in all respects correct and true except as to the objections theretofore made and filed by him, and a stipulation dated March 31, 1941, of all the parties who have appeared herein concerning the allocation to principal or income of numerous items of expenditures having been made and filed herein, and the affidavits of George F. Culhane and Thomas W. Harland, each duly sworn to on the 31st day of March, 1941, having been filed herein together with a stipulation of all the parties who have appeared herein, dated the 31st day of March, 1941, that if said persons were called as witnesses in this proceeding they would testify to the facts as stated in said respective affidavits and that said affidavits might be admitted in evidence in this proceeding, and the said Surrogate having rendered and filed his decision in writing herein published in the New York Law Journal on the 9th day of April, 1941, and in said second and third decisions of said Surrogate hereinabove mentioned said Surrogate having determined that said objections filed herein of said special guardian numbered I, II, III, IV, V and VII should be overruled and said objection numbered VI filed by said special guardian should be sustained in part; that certain items of expenditures set forth in said account should be charged to income instead of principal as capital improvements and that said account be adjusted as more particularly hereinafter set forth, and in all other respects said objection numbered VI of said special guardian should be [fol. 19] overruled and that said objections numbered 1 to 15, inclusive, filed on behalf of said Emma M. West should be overruled; it is

**Ordered, Adjudged and Decreed:**

5. That said objections filed herein by said special guardian numbered I, II, III, IV, V, and VII, and also numbered VI, excepting only as to the items herein mentioned in paragraphs 8 to 14, inclusive, hereof be and the same hereby are overruled.

6. That said objections numbered 1 to 15 filed herein on behalf of said Emma M. West be and the same hereby are overruled.

7. That said objection numbered VI filed by said special guardian be and the same hereby is sustained with respect to the items of said account hereinafter mentioned in paragraphs 8 to 14, inclusive, hereof.

8. That the following items of expenditures set forth in Schedule Cb of said account which were made by accountant during the second fiscal year of the operation of premises known as 46 Noll Street, Brooklyn, New York, to wit:

July 6, 1936 Repairing windows and furnishing and installing cellar door	\$25.00
Dec. 12, 1936	5.00
Jan. 6, 1937 Repairs to heating and plumbing (part of \$16.00)	8.00
Jan. 6, 1937 Electric fixtures and switches installed (part of \$22.00)	11.00
Feb. 9, 1937	30.00

be and they hereby are charged to the income derived from [fol. 20] said premises and Schedule Cb of said account be and the same hereby is adjusted by increasing the item of carrying charges on said property appearing on page 15 thereof for said fiscal year from \$385.34 to \$464.34; by increasing the total of all carrying charges on said premises appearing on page 15 thereof from \$3,085.11 to \$3,164.11, by increasing the net deficit from the operation of said premises appearing on page 15 thereof for said fiscal year from \$24.34 to \$103.34; by increasing the total of all net deficits appearing on pages 15 and 16 thereof from \$544.64 to \$623.64; by decreasing the item of capital improvements appearing on page 15 thereof for said fiscal year from \$246 to \$167; and by decreasing the total of all capital improvements appearing on pages 15 and 16 thereof from \$1,538.37 to \$1,459.37.

9. That the following item of expenditure set forth in Schedule Cd of said account which was made by accountant during the first fiscal year of the operation of premises known as 2022 East 9th Street, Brooklyn, New York, to wit:

July 9, 1936	\$8.00
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be and it hereby is charged to the income derived from said premises and Schedule Cd of said account be and the same hereby is adjusted by increasing the item of carrying

charges appearing on page 16 thereof from \$364.48 to \$372.48; by increasing the total of all carrying charges on said premises appearing on page 16 thereof from \$2,627.21 to \$2,635.21; by increasing the net deficit from the operation of said premises appearing on page 15 thereof for said fiscal year from \$364.48 to \$372.48; by increasing the total [fol. 21] of all net deficits appearing on pages 16 and 17 thereof from \$2,557.21 to \$2,565.21; by decreasing the item of capital improvements appearing on page 15 thereof for said fiscal year from \$80.38 to \$72.38; and by decreasing the total of all capital improvements appearing on pages 16 and 17 thereof from \$107.38 to \$99.38.

10. That the following items of expenditures set forth in Schedule Cf of said account which were made by accountant during the first fiscal year of the operation of the premises known as 1441-3 66th Street, Brooklyn, New York, to wit:

Oct. 30, 1936	\$14.00
Jan. 29, 1936	25.00
Feb. 19, 1936	13.75
Mar. 30, 1936	35.00

be and they hereby are charged to the income derived from said premises and Schedule Cf of said account be and the same hereby is adjusted by increasing the item of carrying charges expended on said property appearing on page 15 thereof for said fiscal year from \$463.61 to \$551.36; by increasing the total of all carrying charges on said premises appearing on page 15 thereof from \$2,825.28 to \$2,913.03; by decreasing the net rents from the operation of said premises appearing on page 15 thereof for said fiscal year from \$309.89 to \$222.14; by decreasing the total of all net rents appearing on page 15 thereof from \$1,234.57 to \$1,146.82; by decreasing the amount of net rents in excess of 3% per annum for said fiscal year appearing on page 15 thereof from \$174.89 to \$87.14; by decreasing the total of the amount of net rents in excess of 3% appearing on pages [fol. 22] 15 and 16 thereof from \$395.36 to \$307.61; by decreasing the item of capital improvements appearing on page 15 thereof for said fiscal year from \$555.22 to \$467.47; and by decreasing the total of all capital improvements appearing on pages 15 and 16 thereof from \$559.22 to \$471.47.



11. That the following items of expenditures set forth in Schedule Cg of said account which were made by accountant during the first fiscal year of the operation of premises known as 2047 East 27th Street, Brooklyn, New York, to wit:

Sept. 1, 1936 Glass and sash chains in windows	\$3.50
Dec. 2, 1936	2.00
Dec. 29, 1936	3.50

and the following items in said schedule, which expenditures were made by accountant during the second fiscal year of the operation of such property, to wit:

Jan. 22, 1937	\$10.60
Mar. 27, 1937	19.00

be and they hereby are charged to the income derived from said premises and Schedule Cg of said account be and the same hereby is adjusted by increasing the items of carrying charges expended on said property appearing on page 12 thereof for said first and second fiscal years from \$244.27 and \$371.98 to \$253.27 and \$401.58, respectively; by increasing the total of all carrying charges on said premises appearing on page 12 thereof from \$1,649.20 to \$1,687.80; by decreasing the net rents derived from said premises appearing on page 12 thereof for said first and second fiscal years [fol. 23] from \$250.73 and \$95.52 to \$241.73 and \$65.92, respectively; by decreasing the total of all net rents derived from the operation of said premises appearing on page 12 thereof from \$507.68 to \$469.08; by decreasing the amount of rents in excess of 3% for said first fiscal year from \$123.23 to \$114.23; by decreasing the total of excess rents over 3% appearing on pages 12 and 13 thereof from \$123.23 to \$114.23; by decreasing the amount of net rents transferred to income for said second fiscal year, appearing on page 12 thereof, from \$95.52 to \$65.92; and by decreasing the total of all net rents transferred to income appearing on page 12 thereof, and also on page 13 of Schedule All, from \$340.19 to \$310.59; by decreasing the items of capital improvements appearing on page 12 thereof for said first and second fiscal years from \$344.56 and \$198.38 to \$335.56 and \$168.78, respectively; and by decreasing the total of all capital improvements appearing on pages 12 and 13

thereof from \$461.91 to \$423.31; by decreasing the item of advances during the accounting period appearing on page 13 thereof from \$177.08 to \$147.48 and by decreasing the item of all amounts advanced to the date of the account from principal appearing on page 13 thereof and also on page 4 of Schedule H from \$1,943.91 to \$1,914.31.

12. That the following item of expenditure set forth in Schedule Ch of said account which was made by accountant during the first fiscal year of the operation of premises known as 240 Floyd Street, Brooklyn, New York, to wit:

Sept. 5, 1936

\$15.06

[fol. 24] be and it hereby is charged to the income derived from said premises and Schedule Ch of said account be and the same hereby is adjusted by increasing the amount of carrying charges expended on said property appearing on page 14 thereof for said fiscal year from \$460.46 to \$475.46; by increasing the total of all carrying charges on said premises appearing on page 14 thereof from \$1,910.23 to \$1,925.23; by decreasing the net rents from the operation of said premises appearing on page 14 thereof for said fiscal year from \$31.54 to \$16.54; by decreasing the total of all net rents appearing on page 14 thereof from \$248.88 to \$233.88; by decreasing the amount of net rents transferred to income appearing on page 14 thereof for said fiscal year from \$31.54 to \$16.54; by decreasing the total of all net rents transferred to income appearing on page 14 thereof and also on page 13 of Schedule A-2 from \$149.43 to \$134.43; by decreasing the item of capital improvements appearing on page 14 thereof for said fiscal year from \$303.52 to \$288.52; by decreasing the total of all capital improvements appearing on pages 14 and 15 thereof from \$412.02 to \$397.02; by decreasing the item of amounts advanced during the accounting period appearing on page 15 thereof from \$413.09 to \$398.09; and by decreasing the item of all amounts advanced to the date of the account appearing on page 15 thereof and also on page 4 of Schedule H from \$1,262.88 to \$1,247.88.

13. That the following item of expenditure set forth in Schedule Cj of said account which was made by accountant [fol. 25] during the first fiscal year of the operation of

premises known as 41 Montrose Avenue, Brooklyn, New York, to wit:

Mar. 9, 1937

\$10.50

and the following items in said schedule, which expenditures were made by accountant during the second fiscal year of the operation of such property, to wit:

Feb. 10, 1938 Repairs to plumbing (part of \$19) \$12.00

Feb. 10, 1938 General repairs to 2nd floor apt.

to put in tenantable condition 15.99

be and they hereby are charged to the income derived from said premises and Schedule Cj of said account be and the same hereby is adjusted by increasing the items of carrying charges expended on said property appearing on page 13 thereof for said first and second fiscal years from \$462.15 and \$594.84 to \$472.65 and \$622.83, respectively; by increasing the total of all carrying charges on said premises appearing on page 13 thereof from \$1,382.85 to \$1,421.34; by increasing the net deficit from the operation of said premises appearing on page 13 thereof for said first fiscal year from \$208.15 to \$218.65; by decreasing the amount of net rents derived from said premises during said second fiscal year from \$164.16 to \$136.17; by decreasing the net rent throughout said operation appearing on pages 13 and 14 thereof from \$113.35 to \$74.86; by decreasing the items of capital improvements appearing on page 13 thereof for [fol. 26] the said first and second fiscal years from \$1,008.59 and \$347.24 to \$998.09 and \$319.25, respectively; by decreasing the total of all capital improvements appearing on pages 13 and 14 thereof from \$1,355.83 to \$1,317.34.

14. That Schedule AII of said account, at page 13 thereof, be and the same hereby is adjusted by decreasing the total amount of net rents from foreclosed properties transferred to income from \$2,212.94 to \$2,168.34; and by decreasing the amount of income shown to be received by said accountant, on page 13 of Schedule AII, from \$28,966.49 to \$28,921.89, and that Schedule H at page 4 be adjusted by decreasing the cash overdraft appearing thereon from \$155.70 to \$111.10 and by increasing the balance of principal on hand appearing thereon from \$123,078.40 to \$123,118.00; and that Schedule III of said account, at page 1 thereof, be adjusted by decreasing the amount of cash constituting in-

come remaining in the hands of accountant from \$2,724.66 to \$2,680.06 and the total amount of income shown to be on hand from \$3,132.05 to \$3,087.45.

15. That as so adjusted hereinabove, said account properly credits or charges to income or principal, as the case may be, all sums received or paid out by said accountant and properly apportions between income and principal the proceeds of sale and other sums received in connection with the ownership or sale of properties acquired by said accountant upon foreclosure of mortgages held as a part of the principal of said trust or by deed in-lieu of such foreclosure.

[fol. 27] And the said matter having been duly adjourned to this day the said Surrogate after having duly examined said account now here finds the state and condition of said account to be as set forth in the following Summary Statement thereof made by the Surrogate as judicially adjusted, settled and allowed by him to be recorded with and taken to be a part of the decree in this matter, to wit:

A Summary Statement of the account of proceedings of City Bank Farmers Trust Company, as trustee under the last will and testament of Henry C. West, deceased, to and including the 31st day of July, 1940, made by the Surrogate as judicially adjusted, settled and allowed.

#### AS TO PRINCIPAL

##### *Accountant is charged as follows:*

With amount of all property originally received to constitute principal, as shown in Schedule "A".....	\$132,753 26	
With amount of increases as shown in Schedule "A1".....	10 50	
With amounts refunded to principal on account of advances (made by executor) for foreclosure expenses, etc., as follows:		
Premises 193 Bay 17th Street, Brooklyn, N. Y. as shown in Schedule "Ce", page 12.....	\$29 16	
Premises 1441-3 66th Street, Brooklyn, N. Y., as shown in Schedule "Cf", page 16.....	311 72	340 88
Forward.....		\$133,104 64
[fol. 28] Brought forward.....		\$133,104 64

*Accountant is credited as follows:*

With amount of decreases, as shown in Schedule "B".....	\$5,186.12		
With amount of payments for administration expenses, chargeable against principal, as shown in Schedule "C".....		766.76	
With amounts advanced (since May 13, 1936) from principal in connection with the following properties all situated in Brooklyn, N. Y., acquired by foreclosure or by deed in lieu of foreclosure as adjusted:			
Premises 46 Noll Street, as shown in Schedule "Cb", page 16.....	\$751.68		
Premises 1855 East 7th Street, as shown in Schedule "Cc", page 12..	420.98		
Premises 2022 East 9th Street, as shown in Schedule "Cd", page 17..	2,315.53		
Premises 2047 East 27th Street, as shown in Schedule "Cg", page 13 as adjusted.....	147.48		
Premises 240 Floyd Street, as shown in Schedule "Ch", page 15 as adjusted.....	398.00	4,033.76	9,986.64
Leaving a balance of principal on hand of.....			\$123,118.00
consisting of the property set forth in Schedule "H" carried at inventory value of \$123,229.10, subject to a cash overdraft of \$111.10.			

*As to INCOME**Accountant is charged as follows:*

With amount of all income received, as shown in Schedule "AII" as adjusted.....		\$28,921.89	
Forward.....		\$28,921.89	
[fol. 29] Brought forward.....		\$28,921.89	

*Accountant is credited as follows:*

With amount of all payments for necessary expenses, including commissions, chargeable against income, as shown in Schedule "CII".....	\$1,154.99		
With amount of all payments to or for the account of beneficiaries from income, as shown in Schedule "FI".....	24,679.45	25,834.44	
Leaving a balance of income on hand of.....		\$3,087.45	
consisting of \$2,680.06 in cash and securities of \$407.39, as set forth in Schedule "HI" as adjusted.			

And It Appearing that said accountant has fully accounted for all the moneys and property of said trust estate which have come or should have come into its hands as trustee as aforesaid during the period covered by said account, and said account having been duly adjusted by the said Surrogate and a Summary Statement of the same having been made as above and herewith recorded; it is

Ordered, Adjudged and Decreed:

16. That the said account be and the same hereby is judicially settled and allowed in all respects as filed and adjusted.



17. That said accountant has collected all of the assets of said trust estate which were collectible by it from the 31st day of July, 1940, and that in said account accountants have charged themselves with all moneys or property received by them and interest on all sums for which they should be charged and all sums with which said accountants have [fol. 30] credited themselves in said account were properly credited for moneys properly paid out by them for reasonable and necessary expenses, for losses incurred by them without fault on their part, or for moneys properly distributed by them and paid out by them to the beneficiaries of said trust estate.

18. That out of the balance of principal so found as above remaining in its hands the said accountant retain and pay unto itself the sum of One thousand three hundred fifty-six and 81/100 dollars (\$1,356.81) as and for the commissions on principal to which it is entitled on this accounting for receiving the sum of One hundred thirty-two thousand seven hundred sixty-three and 76/100 dollars (\$132,763.76) and for paying out the sum of Seven hundred sixty-six and 76/100 dollars (\$766.76).

19. That out of the balance of income so found as above remaining in its hands said accountant retain and pay unto itself the sum of Three hundred sixty-two and 26/100 dollars (\$362.26) as and for the commission on income to which it is entitled upon this accounting for receiving and paying out the sum of Thirty-nine thousand seven hundred seven and 50/100 dollars (\$39,707.50).

20. That out of the balance of principal so found as above remaining in its hands said accountant retain and pay unto itself the sum of Forty-six and 70/100 dollars (\$46.70) as and for its disbursements as taxed herein; and that it pay to Emma M. West, or to Messrs. Larkin, Rathbone & Perry, her attorneys, the sum of Five hundred and 00/100 dollars [fol. 31] (\$500.00) as hereby allowed by the Surrogate for her counsel fees and other expenses necessarily incurred herein; and to Marie Elizabeth West Jones and Elizabeth Frances Jones, or their attorneys, Messrs. Butler, Wyckoff and Reid, the sum of Three hundred fifty and 00/100 dollars (\$350.00) as hereby allowed by the Surrogate for their counsel fees and other expenses necessarily incurred herein; and to Gerald P. Calkin, Esq., the sum of One thousand

five hundred and 00/100 dollars (\$1,500.00), which amount is hereby awarded to him for his services as special guardian in this proceeding.

21. That City Bank Farmers Trust Company, as trustee as aforesaid, after carrying out the provisions of this decree continue to hold and administer the balance of the property remaining in its hands constituting the principal of said trust as set forth above upon the trusts more particularly set forth in said will.

And It Appearing that the above mentioned balance of income remaining in the hands of said accountant after making the payment and deduction hereinbefore directed will consist of the sum of Two thousand three hundred seventeen and 80/100 dollars (\$2,317.80) in cash and a Four hundred seven and 39/100 dollars (\$407.39) interest in the bond and mortgage of Carmine Marrone covering premises known as 41 Montrose Avenue, Brooklyn, New York, in the principal amount of Three thousand two hundred dollars (\$3,200), upon which, on July 31, 1940, there was due the sum of Three thousand and fifty dollars (\$3,050.00), which said interest is subordinate in lien to a prior interest originally of One thousand twenty-three and 51/100 dollars (\$1,023.51) due to principal upon which [fol. 32] there remained unpaid on July 31, 1940, the sum of Eight hundred seventy-three and 51/100 dollars (\$873.51); it is

Ordered, Adjudged and Decreed:

22. That City Bank Farmers Trust Company pay and transfer to said Emma M. West said balance of income remaining in its hands after making the aforesaid payment and deduction hereinbefore directed so far as the same consists of cash, to wit, the sum of Two thousand three hundred seventeen and 80/100 dollars (\$2,317.80).

23. That upon complying with the provisions of this decree said City Bank Farmers Trust Company in its individual capacity and as trustee of the trust created under the last will and testament of said Henry C. West, deceased, be and it hereby is discharged from any and all responsibility, liability or accountability with respect to or by reason of any matter or thing set forth in the account herein or in this decree except that said City Bank Farmers Trust Company shall remain accountable for the balance of principal

and said subordinate interest in said bond and mortgage remaining in its hands after carrying out the provisions of this decree.

And It Further Appearing that said trust estate consisted of bonds and mortgages acquired by testator and that certain of these mortgages were foreclosed by accountant as executor or as trustee and the property covered by said mortgages was purchased by accountant upon the foreclosure sale and that in certain instances a deed in lieu of such foreclosure was taken by accountant as such executor or [fol. 33] trustee; that, in all, nine separate parcels of real property so acquired have been held by said trustee and that said trustee expended sums of money in the acquisition of said parcels and further sums of money during the respective periods of ownership thereof and that rents were received from said premises by said trustee; that two of said parcels were sold prior to April 13, 1940, and that seven of such parcels remained in the hands of the trustee at the date of the account rendered and filed herein; that the trust estate remaining in the hands of accountant at the date of such account consists in part of mortgages so acquired by testator; that Bond and Mortgage Guarantee Company had guaranteed the payment of principal and interest of the obligations secured by certain of such bonds and mortgages and that while the interest upon such obligations was collected by said company, it deducted therefrom as a charge for the guarantee in each year one-half of one per centum of the principal amount secured; that said Bond and Mortgage Guarantee Company is now in liquidation and that the agency of said company as to each of the bonds and mortgages under which the respective properties were acquired by accountant was terminated by accountant prior to such acquisition; that after such termination of the agency of Bond and Mortgage Guarantee Company said accountant agreed with the owner of premises known as 240 Floyd Street, Brooklyn, New York, that the interest rate on the obligations secured by the mortgage then held by said accountant covering said premises should be reduced to four per centum per annum and that thereafter said mortgage was foreclosed and accountant purchased said property at the foreclosure sale and continued to hold said [fol. 34] property at the date of its account herein; that in

the proceeding for the liquidation of Bond and Mortgage Guarantee Company said accountant filed claims with respect to each of the bonds and mortgages under which properties were so acquired covering the period to December 31, 1937, the date as of which the rights of the parties in such liquidation proceeding were fixed, and said claims have been allowed in said liquidation proceeding and dividends upon such claims will be received by accountant hereafter; that no decree or judgment of any court or agreement or action by any of the parties has determined the method of computation of net rents or of apportionment and allocation thereof or of the proceeds of sale of such property or of the amounts which may be received upon such guaranties between income and principal of said trust estate whether such property had been so acquired prior to the date of such account or have been or may hereafter be so acquired by accountant subsequent to such date or whether such rents were received before the date of said account or have been or may hereafter be received subsequent thereto; that the will of Henry C. West under which said trust was created directs the trustee to apply the net income from the trust estate to the use of the persons therein named; that said will contains no express provision directing the manner of computation of net rents from properties so acquired by said trustee upon foreclosure of mortgages or by deed in lieu thereof or the apportionment and allocation of such rents or of the proceeds of sale of such properties of the amounts which may be received upon such guaranties; and, that the said trustee in its petition herein has prayed that this court construe the last will and testament of said Henry [fol. 35] C. West, deceased, with respect to such matters and for instructions by this court with respect thereto, as is more fully set forth in said petition; it is

Ordered, Adjudged and Decreed:

24. (a) The accountant, as trustee under the last will and testament of Henry C. West, deceased, has acquired upon the foreclosure, or by deed in lieu of foreclosure, of mortgages held by it on or prior to April 13, 1940, and now holds, the following parcels of real property:

46 Noll Street, Brooklyn, New York.

1855 East 7th Street, Brooklyn, New York.

2022 East 9th Street, Brooklyn, New York.

193 Bay 17th Street, Brooklyn, New York.

1441-3 66th Street, Brooklyn, New York.  
 2047 East 27th Street, Brooklyn, New York.  
 240 Floyd Street, Brooklyn, New York.

(b) Each of such parcels and each parcel of real property hereafter acquired by the trustee, either upon foreclosure or by deed in lieu of foreclosure of a mortgage so held by it on April 13, 1940, covering the same, shall be held by the trustee upon a separate trust to sell the same. For the purpose of apportioning the rents and income and proceeds of sale received from said parcels, the trustee shall maintain a separate account with respect to each such parcel, reflecting separately the principal and income charges and credits as hereinafter provided. Said accounts shall be kept on a cash rather than an accrual basis, i. e., receipts shall be credited when received and payments shall be charged when made, irrespective of the time when such receipts and expenses may have accrued.

[fol. 36] (c) For the purposes of this Article 23 of this decree, and with respect to each such parcel of real property, (1) the term "principal of the mortgage" shall be deemed the principal amount of the mortgage covering each such parcel of real property, which remained due and was secured to be paid by said mortgage immediately prior to the foreclosure thereof or the acquisition of such property by deed in lieu of foreclosure, and (2) the term "mortgage rate" shall be deemed to be the full rate of interest payable on the principal of the mortgage covering such parcel of real property immediately prior to the foreclosure of said mortgage or the acquisition of such property by deed in lieu of foreclosure; that is to say: if the rate of interest provided in the mortgage was reduced by the trustee prior to the foreclosure or acquisition by deed in lieu of foreclosure, the mortgage rate shall be the rate to which the same was reduced by the trustee; if the mortgage was guaranteed, no allowance shall be made for the sum deducted from the interest payable on the principal of said mortgage by the guarantor, but the full rate provided to be paid by the mortgagor shall be deemed the mortgage rate. Accordingly, the mortgage rate with respect to each of the following parcels shall be the rate set opposite the same below, to wit:

46 Noll Street, Brooklyn, New York  
 1855 East 7th Street, Brooklyn, New York

6%  
 6%



2022 East 9th Street, Brooklyn, New York	6%
193 Bay 17th Street, Brooklyn, New York	6%
1441-3 66th Street, Brooklyn, New York	6%
2047 East 27th Street, Brooklyn, New York	6%
240 Floyd Street, Brooklyn, New York	4%

(d) The income account with respect to each said parcel shall be kept on an annual fiscal year basis. The first day [fol. 37] of each such fiscal year shall be the date of acquisition of such property or the anniversary thereof.

(e) The rents and other income, if any, collected during each such fiscal year from said parcel shall be credited to the income account with respect thereto, and all ordinary expenses incurred in the operation of such property and paid during such year shall be charged against said income account.

(f) All other expenses incurred in the acquisition or the operation of such property shall be charged against the principal account with respect to said parcel; included among the sums so chargeable against principal which shall not be deemed ordinary operating expenses are the following: All expenses incurred in connection with the foreclosure or in securing a conveyance in lieu of foreclosure; all taxes upon such parcel and other liens which accrued prior to the date of acquisition of such property by the trustee; and the cost of all capital improvements; if because of the use or neglect of such property prior to the acquisition thereof it is not in a rentable condition when acquired, the cost of rehabilitation, that is, the expenses necessary to put the property in a state of repair reasonably commensurate with its type and location in order to be rentable for its reasonable value, are chargeable to principal as part of the cost of capital improvements.

(g) At the close of each fiscal year the net income from the operation of each such parcel during such year as determined by such income account shall be computed.

[fol. 38] (h) The net amount of the income from each such parcel in each such fiscal year up to but not exceeding three per centum of the principal of the mortgage shall be deemed to be income of the trust and shall be credited to the income account of the general trust estate. Any bal-

ance of such income shall be credited to the principal account with respect to such property and shall be used to repay advances from principal hereinafter authorized to be made and if such advances be entirely repaid, such income shall be impounded (subject to reinvestment as any other principal pursuant to the terms of the will) to await the sale of said premises and apportionment with such proceeds of sale. Said sums of income are hereinafter referred to as "net rents credited to income" or "principal," respectively. Any income derived from any sum so impounded shall be deemed to be and shall be distributed as income of the general trust estate.

(i) Upon the sale of each such parcel by the trustee, the balance of income, if any, standing to the credit of the income account with respect to such property representing the net income from such property during the fiscal year in which the same is sold, shall be distributed between principal and income by crediting to income so much thereof as may be equal to but shall not exceed interest on the principal of the mortgage at the rate of three per cent. per annum for the period commencing at the first of said fiscal year and ending on the date the sale of said premises is closed, and by crediting the principal the balance, if any, of said net income. The sums so credited to principal and income shall be held and disposed of in the same manner as the sums [fol. 39] credited to principal and income pursuant to paragraph (h) hereof.

(j) If at the end of any fiscal year, or upon such sale, it is determined from such income account with respect to any such parcel, that it has been operated at a deficit during such fiscal year, or part thereof, such deficit shall be charged to the principal account with respect to such parcel.

(k) Any income from any of such parcels of real property credited to the income account of the general trust estate as provided in paragraphs (h) and (i) hereof, shall be treated as any other income of the trust estate and shall be distributable by the trustee as such to the person or persons entitled to receive such income, and such trustee shall not be subject to surcharge by reason of distributing any such income, even if upon the sale of such property it shall appear that the income beneficiary or beneficiaries shall have received more than such beneficiary or beneficiaries

would otherwise be entitled to receive as income from such property, nor shall the trustee or any other person interested in the trust fund be entitled to recoup any part of the income from any of said parcels of real property distributed to the income beneficiary or beneficiaries as herein provided.

(l) Pending the sale of each such parcel of real property by the trustee, any sums chargeable against the principal account with respect thereto may be advanced by the trustee out of the principal of the general trust estate. If at any time the expenses of operation of any such parcel exceed the balance credited to the income account with respect [fol. 40] thereto, the amount required to pay such expenses may be advanced from the principal of the general trust estate.

(m) Any amounts of income from any such parcel credited to the principal account with respect thereto, pursuant to paragraphs (h) and (i) hereof shall be applied first in discharge of the sums charged to the principal account with respect to such parcel. The principal of the trust estate shall have a first lien against the proceeds of sale of each such parcel for any sum of principal advanced as provided in this article in connection with such parcel, and not repaid from the income collected from such parcel, hereinafter in this article referred to respectively as "principal advances," and "the balance of principal advances."

(n) Upon the sale of each such parcel by the trustee, the proceeds thereof after first deducting the expenses of such sale plus the balance of net rents credited to principal in excess of principal advances, if any, shall be distributed between principal and income as follows:

(i) There shall first be deducted therefrom and transferred to principal the balance of principal advances, if any. The balance remaining is hereinafter referred to as the "balance for distribution."

(ii) For purposes of apportionment there shall be added to the balance then remaining all net rents credited to income.

(iii) The resulting sum shall be apportioned between principal and income in the proportions which the principal amount set forth in subdivision (a) below and the

[fol. 41] income amount set forth in subdivision (b) below bear to each other:

(a) the principal amount shall be the principal of the mortgage, and, if interest from a date prior to the death of the decedent was unpaid, there shall be added thereto interest at the mortgage rate on the principal of the mortgage from the last day to which interest was paid thereupon to the date of the death of the decedent; and

(b) the income amount shall be interest at the mortgage rate on the principal of the mortgage from the date of death of the decedent or from the last date to which interest was paid on said mortgage, whichever date shall be later, to the date of sale of the respective premises by the trustee.

(iv) From the amount so apportioned to income there shall be deducted the net rents credited to income of the general trust estate and the balance so apportioned to income shall be credited to income of the general trust estate out of the balance for distribution and is hereinafter referred to as "the income share of the balance for distribution"; if the net rents credited to income shall be equal to or exceed the amount so apportioned to income, income shall receive no further sum; the remainder of the balance for distribution (or all thereof, as the case may be) shall be credited to principal of the general trust estate and is hereinafter referred to as "the principal share of the balance [fol. 42] for distribution."

(o) If part of the proceeds of sale of any such parcel of real property shall consist of a purchase money mortgage, then any cash and such purchase money mortgage representing net proceeds of such sale and net rents credited to income in excess of principal advances, if any, shall be distributed as follows:

(i) The cash, if sufficient, shall be utilized to repay the balance of principal advances.

(ii) After such repayment of principal advances, if the balance for distribution consists of cash and a purchase money mortgage, such cash and such purchase money mortgage shall each be apportioned be-

tween and credited to principal and income in the proportions, which the principal share of the balance for distribution and the income share of the balance for distribution shall bear to each other.

(iii) If such cash is not sufficient to discharge in full the balance of principal advances as set forth in subdivision (i) of this paragraph (o), then the principal of the trust estate shall have a first lien upon such purchase money mortgage for the balance of such principal advances, and any sums paid on account of the principal of said purchase money mortgage shall first be used to pay and discharge said lien. Any further payments on account of said purchase money mortgage shall be apportioned between principal and income in [fol. 43] proportion to their respective interests therein.

(iv) Any interest received on any such purchase money mortgage shall be deemed to be income earned by the trust estate and distributable as such.

25. That any sums which may be received upon the claims which have been allowed to the trustee in the proceeding for the liquidation of Bond and Mortgage Guarantee Company on account of the guaranty of mortgages with respect to which real property was heretofore acquired shall be apportioned between principal and income as follows:

(a) It shall be presumed that that amount of the respective allowances made in said proceeding which is equal to the amount of unpaid interest secured by the respective guaranties, or all thereof if the allowance be less than such unpaid interest, is allowance on account of loss of interest and the balance, if any, is allowance on account of loss of principal; of such allowance on account of loss of interest only that part representing loss of interest since the date of death of the decedent shall be considered allowance for loss of income for purposes of apportionment by the trustee.

(b) The allowances made in said proceeding for claims with respect to the guaranty of the obligations secured by the mortgages covering the below described premises shall be deemed to be allowance on account



of loss of income and allowance on account of loss of principal in the amounts set forth below, to wit:

[fol. 44]	Principal allowance	Income allowance
46 Noll Street, Brooklyn, N. Y.	\$2,873.92	\$ 806.67
1855 East 7th Street Brooklyn, N. Y.	\$1,882.36	\$1,411.67
2022 East 9th Street, Brooklyn, N. Y.	\$4,209.41	\$1,383.75
193 Bay 17th Street, Brooklyn, N. Y.	\$ 110.85	\$1,008.33
1441-3 66th Street, Brooklyn, N. Y.	0.00	\$ 532.59
2047 East 27th Street, Brooklyn, N. Y.	\$2,436.17	\$ 857.08
240 Floyd Street, Brooklyn, N. Y.	\$1,088.42	\$ 465.00

(c) If any sums shall be paid to said trustee upon such claims prior to the sale of the respective premises, such payment shall be apportioned between principal and income in the proportion which the allowance on account of loss of principal bears to the allowance on account of loss of income; the amount so apportioned to income shall be credited on the date received by the trustee to the respective separate income accounts hereby directed to be maintained by accountant in Article 23 hereof and shall be treated in the same manner as ordinary income from the respective properties. The amount apportioned to principal shall be credited to such respective separate principal accounts and shall be treated in the same manner as a payment to such account of income in excess of three per centum of the principal amount secured by the mortgage as hereinbefore directed in Article 23 hereof.

[fols. 45-47] (d) If any sums shall be paid to said trustee upon such claims after the sale of the respective premises, such payment shall be apportioned between principal and income in the proportions specified in subdivision (iii) of paragraph (n) of Article 23 hereof for the apportionment of the proceeds of sale of

and net income from the respective properties and shall be credited accordingly to the principal and income accounts of the general trust estate.

26. That the salvage operations with respect to premises known as 168 Morrison Avenue, West New Brighton, Staten Island, New York, and 41 Montrose Avenue, Brooklyn, New York, were completed by the sale of the premises on August 25, 1939 and August 9, 1939, respectively, and since such operations were completed prior to April 13, 1940, the date on which Chapter 452 of the Laws of 1940 (Section 17-c of the Personal Property Law) became a law the allocation and apportionment of the rents derived therefrom and the proceeds of sale thereof were not affected in any way by the enactment of said law.

James A. Foley, Surrogate.

[fol. 48] IN SURROGATE'S COURT, COUNTY OF NEW YORK

PETITION FOR JUDICIAL SETTLEMENT OF TRUSTEE'S ACCOUNT:  
FOR CONSTRUCTION OF WILL; AND FOR INSTRUCTIONS AND  
DIRECTIONS

To the Surrogate's Court of the County of New York:

The petition of City Bank Farmers Trust Company as trustee under the last will and testament of Henry C. West, deceased, respectfully shows to this Court, upon information and belief:

1. Your petitioner is a domestic corporation having its principal office and place of business at No. 22 William Street, in the Borough of Manhattan, City, County and State of New York, and prior to June 28, 1929, was known as The Farmers' Loan and Trust Company.

2. Henry C. West died on the 1st day of May, 1934, a resident of the City, County and State of New York. Said decedent left a last will and testament bearing date the 14th day of December, 1928, which was duly admitted to probate by the Surrogate's Court of the County of New York; to which jurisdiction in that behalf belonged, on the 28th day of May, 1934. A copy of said last will and testament is

annexed to the account of proceedings of your petitioner, herewith filed.

3. Said testator in and by the "Fifth" and "Eighth" clauses of his will provided as follows:

[fol. 49] "Fifth: All the rest, residue and remainder of my estate, both real and personal, wheresoever situate, of which I may die seized or possessed, or to which I may be entitled at the time of my death, I give, devise and bequeath to The Farmers' Loan and Trust Company, a corporation organized and existing under the laws of the State of New York, in Trust, Nevertheless, for the following uses and purposes: To lease said real property and collect the rents thereof, and to invest and from time to time in its discretion reinvest the personal property in such securities as to it may seem proper; to collect the rents, issues and profits of all of my said residuary estate, and, after paying all necessary charges of administration, to apply the net income from said estate to the use of my wife, Emma M. West, during the term of her natural life, or until she shall remarry.; Provided, However, that during the life of my said wife, Emma M. West, but not after her death, there shall be first applied out of the said net income the sum of One hundred dollars (\$100.) per month to the use of my brother, Zimri West. If my said wife shall remarry, the aforesaid payment to my said brother shall continue to be made as long as my said wife lives.

Upon the death or remarriage of my said wife, my Trustee shall set aside from my residuary estate cash or securities having a then value of Thirty thousand dollars (\$30,000.) and shall continue to hold and administer the same, In Trust, and shall pay or apply [fol. 50] the net income therefrom to the use of my nephew, Zimri West, 3rd, during the term of his life, and upon his death shall transfer and pay over the principal of such trust fund to my grandniece, Elizabeth Frances Jones, if she is then living, or, if she shall then be dead, shall transfer and pay over the same in equal shares per stirpes to and among her issue then living. The balance of my said residuary estate my Trustee shall continue to hold and administer, In Trust, to pay or apply the net income therefrom to or for the

use of my niece, Marie Elizabeth West Jones, during the term of her life and upon her death shall transfer and pay over one-third of the principal of such trust fund to her daughter, my grandniece, Elizabeth Frances Jones, or if she shall then be dead, to her issue then living in equal shares per stirpes, and shall transfer and pay over the remaining two-thirds of such trust fund in equal shares per stirpes to the issue then living of my wife's niece, Wealthy Albro Lewis Demorest. If, pursuant to the foregoing provisions of this my will, any part of my estate shall have been held in trust for a period of two lives and shall not therefore by law be eligible to be continued in trust for an additional period as directed by this Will, such part of my residuary estate shall, at the expiration of a period of two lives during which it has been held in trust, be transferred and paid over by my Trustee outright, free and discharged of any trust, to the persons otherwise entitled pursuant to the provisions of this Will to receive the [fol. 51] income therefrom. If at any time pursuant to the provisions of this my Will, any part of my property shall not have been effectually devised or bequeathed, I hereby give, devise and bequeath the same at such time to the then living issue of my wife's niece, Wealthy Albro Lewis Demorest.

"Eighth. I nominate, constitute and appoint The Farmer's Loan and Trust Company, a corporation organized and existing under the laws of the State of New York, having its principal place of business at Number Twenty-two William Street, in the Borough of Manhattan, City, County and State of New York, to be the Executor of and Trustee under this my last will and testament, and I direct that no bond or other security shall be required of it for the faithful performance of its duties in either capacity."

4. Letters testamentary on said last will and testament, bearing date the 29th day of May, 1934, were duly issued out of said Court to your petitioner, the executor and trustee therein named. Your petitioner duly qualified as executor of and as trustee under said last will and testament.

5. On or about the 17th day of June, 1935, your petitioner duly filed in the Surrogate's Court of the County of New York, to which jurisdiction in that behalf belonged, an account of its proceeding to the 15th day of May, 1935, as executor as aforesaid, together with a petition praying that [fol. 52] said account be judicially settled and allowed, and on or about the 29th day of June, 1936, your petitioner duly filed in said court a supplemental account of its proceedings to the 13th day of May, 1936, as such executor, together with a supplemental petition praying that said supplemental account be judicially settled and allowed, and such proceedings were thereafter had that on or about the 13th day of August, 1936, a decree of the Surrogate's Court of the County of New York, bearing date the 10th day of August, 1936, was duly made and entered judicially settling and allowing said account and said supplemental account, and directing your petitioner, as such executor, to pay to itself, as such trustee, the balance of principal and income remaining in its hands after making certain payments directed to be made in such decree.

6. Your petitioner, as trustee as aforesaid, duly received the property constituting said trust and has been, and now is, acting as trustee of the trust created under said last will and testament of Henry C. West, deceased.

7. The account of proceedings of your petitioner as trustee under the last will and testament of Henry C. West, deceased, has never been judicially settled and allowed. Accordingly, your petitioner has filed herewith an account of its proceedings to and including the 31st day of July, 1940, to the end that the same may be judicially settled and allowed.

8. Emma M. West, the life beneficiary of the trust created under said last will and testament, is still living and [fol. 53] has not remarried. Zimri West, brother of the decedent, to whose use the sum of One hundred dollars (\$100) per month out of the income of said trust was directed to be applied, died on the 15th day of February, 1940, a resident of the City of Maplewood, County of Essex, State of New Jersey. No legal representative of said Zimri West has been appointed. Said Zimri West was survived by his son, Zimri West, 3rd, and his daughter, Marie Elizabeth West Jones, who are his heirs at-law and next of kin, there



being no other children or children of deceased children nor widow surviving said Zimri West. Your petitioner is informed that said Zimri West left a last will and testament, which has not been admitted to probate, which named said Zimri West, 3rd, executor thereof and sole legatee thereunder:

9. In and by the "Fifth" clause of his will, said testator provided, in part, as follows:

"Fifth. All the rest, residue and remainder of my estate, \* \* \* I give, devise and bequeath to The Farmers' Loan and Trust Company \* \* \* In Trust, Nevertheless, for the following uses and purposes: \* \* \* to apply the net income from said estate to the use of my wife, Emma M. West, during the term of her natural life, or until she shall remarry; Provided, However, that during the life of my said wife, Emma M. West, but not after her death, there shall be first applied out of the said net income the sum of One hundred [fol. 54] dollars (\$100) per month to the use of my brother, Zimri West. If my said wife shall remarry, the aforesaid payment to my said brother shall continue to be made as long as my said wife lives."

Your petitioner is advised by counsel that in their opinion, under the true meaning and construction of said last will and testament, upon the death of the said Zimri West the entire income of said trust should be applied to the use of the said Emma M. West, but that since there may be some doubt with respect thereto, your petitioner should secure the approval of this Court of such construction by application for a judicial determination of the construction and effect of the above quoted portion of the "Fifth" clause of said last will and testament. Your petitioner, therefore, desires that this Court judicially determine the construction and effect of said portion of said last will and testament as to whether the entire income of said trust shall be paid to said Emma M. West during her life or until she shall remarry after the death of said Zimri West.

10. As is shown in Schedule "F" of the supplemental account of your petitioner as executor of the last will and testament of said deceased and in Schedule "A" of the account of your petitioner as trustee, filed herewith, your

petitioner, as trustee, received, as a part of the property constituting said trust, seven certain parcels of real property which had been acquired by your petitioner as such executor upon foreclosure, or by deed in lieu of foreclosure, of mortgages constituting part of the estate of said decedent. [fol. 55] Said parcels of real property are known by and as the street numbers:

46 Noll Street, Brooklyn, New York,  
 190 Bay 17th Street, Brooklyn, New York,  
 240 Floyd Street, Brooklyn, New York,  
 1441-3 66th Street, Brooklyn, New York,  
 1855 East 7th Street, Brooklyn, New York,  
 2022 East 9th Street, Brooklyn, New York,  
 and  
 2047 East 27th Street, Brooklyn, New York.

As is further shown by Schedule "CH" of said account and Schedule "Ca" of said supplemental account of your petitioner, as executor as aforesaid, it was necessary that your petitioner expend certain sums for arrears of taxes, water rents and expenses of foreclosure, or of deed in lieu of foreclosure, and other costs of acquisition, and during the period of ownership it was necessary that your petitioner expend additional sums in payment of taxes, water rents, insurance premiums, improvements, repairs, and other items incurred in the operation of said properties; and on certain of said properties income was received by way of rents. As is shown in said account and supplemental account of your petitioner, as executor as aforesaid, the sums so expended, above the rents received, were temporarily advanced from principal of the estate.

11. With respect to the properties so acquired and to the receipts and disbursements made in connection therewith, the aforesaid decree judicially settling and allowing said account and supplemental account of your petitioner as executor as aforesaid, dated the 10th day of August, 1936, provided as follows:

[fol. 56] "Further Ordered, Adjudged and Decreed that each of the properties received as a result of foreclosure and transferred by said executor to itself as trustee under said decedent's will, be held in a separate account by the trustee, so that all expenses and dis-

bursements incurred in connection with the acquisition of each property as shown in the account and supplemental account herein, together with any and all future receipts and disbursements in connection with each property, may be taken into consideration by the trustee in apportioning the proceeds received upon the ultimate sale of the respective properties between principal and income and that the rights of all persons interested in said trust be and the same hereby are reserved to assert upon any future accounting that any such receipts and disbursements should be taken into consideration by the court in determining the proper apportionment of the proceeds of sale of said properties; and it is

“Further Ordered, Adjudged and Decreed that the amounts herein directed to be paid to said trustee, together with all property heretofore distributed by said executor to itself as trustee, be and the same hereby are made subject to such further taxes and such further expenses in connection with mortgage foreclosures or otherwise as may be payable:”

12. Your petitioner, as trustee as aforesaid, has acquired two certain additional parcels of real property upon foreclosure and by deed in lieu of foreclosure of mortgages con-[fol. 57] stituting a part of the principal of the trust created under the last will and testament of said decedent, and in connection therewith has necessarily expended certain sums for arrears of taxes, water rents and expenses of foreclosure, or of deed in lieu of foreclosure, and other costs of acquisition. Said parcels are known as and by the street numbers:

168 Morrison Avenue, West New Brighton, Staten Island, New York; and

41 Montrose Avenue, Brooklyn, New York.

In connection with the parcels of real property so acquired by your petitioner, as trustee as aforesaid, and in connection with those parcels of real property received by your petitioner, as trustee, from itself, as executor as aforesaid, as is shown in Schedules “Ca” to “Cj” of the account of your petitioner, as trustee as aforesaid, filed herewith, it was necessary that your petitioner expend additional sums in payment of taxes, water rents, insurance

premiums, improvements, repairs, and other items incurred in the operation of said properties, and on certain of said properties income was received by way of rents. As is shown in said account of your petitioner, as trustee as aforesaid, the sums so expended above the rents received were advanced from principal of said trust.

13. Your petitioner has sold and conveyed two of the aforesaid parcels of real property, to wit, premises 168 Morrison Avenue, West New Brighton, Staten Island, New [fol. 58] York, on August 25, 1939, and 41 Montrose Avenue, Brooklyn, New York, on August 9, 1939. As is shown in Schedules "Ci" and "Cj" of the account of your petitioner filed herewith, your petitioner has received the proceeds of sale of said properties which consist, in respect to 168 Morrison Avenue, entirely of cash, and in respect to 41 Montrose Avenue, cash and a purchase money mortgage.

14. Each of the mortgages which covered the parcels of real property so acquired by your petitioner was guaranteed by Bond and Mortgage Guarantee Company, which said company is now in liquidation. As is shown in Schedules "Ca" to "Cj", inclusive, of the account of your petitioner filed herewith, your petitioner has presented in the proceeding for the liquidation of said Bond and Mortgage Guarantee Company claims arising out of the guaranty by said company of each of said mortgages and said claims have been allowed in varying sums. Your petitioner is informed that said claims as allowed will not be paid in full, but that from time to time dividends thereupon will be paid.

15. Your petitioner is advised by counsel that under the true meaning and construction of the will of said decedent, a part of the sums of money or other property received by it as executor or as trustee, or which may hereafter be received by it as trustee as rents from said properties or as proceeds of sale thereof, or upon claims arising out of the guaranty of said mortgages, may constitute income of said trust estate which should be paid to those persons who are now or may hereafter be entitled to the income from said [fol. 59] trust estate, but that there is doubt concerning what proportion, if any, of said rents, proceeds of sale or payments made on account of said claims, may be deemed to be income of the trust created by the will of said testator,

and which now or hereafter should be paid to the persons entitled to the income therefrom, and said counsel further advised your petitioner that it may not safely distribute any part of the sums so received until and unless this Court construes said last will and testament, and determines what proportion, if any, of said rents, proceeds of sale, or moneys received on account of said claims should be distributed as part of the income of the trust estate.

For the convenience of the court your petitioner has included in each of said Schedules "Cb" to "Cj", inclusive, of the account of your petitioner filed herein, a statement of all transactions in connection with each of said premises, and of the facts in connection therewith, and a tentative apportionment between income and principal of the moneys received from said premises by way of rents or proceeds of sale thereof.

16. The names of all persons who are or may be entitled, absolutely or contingently, by the will of Henry C. West, deceased, or by operation of law, to share in the proceeds of the property held by your petitioner as trustee of the trusts created under said last will and testament, together with their places of residence and post office addresses are, as follows:

Emma M. West, widow of the decedent and life beneficiary of the trust, who resides at and whose post office address is 1140 Fifth Avenue, New York, New York.

Zimri West, 3rd, nephew of the decedent and survivor life beneficiary of \$30,000 of the principal of the trust fund, a son of Zimri West, deceased, and one of his heirs at law and next of kin, who is named executor of and sole legatee under the unprobated will of Zimri West, deceased, who resides at and whose post office address is 118 North Grove Street, East Orange, New Jersey.

Marie Elizabeth West Jones, niece of the decedent and survivor life beneficiary of the balance of the principal of the trust fund, a daughter of Zimri West, deceased, and one of his heirs at law and next of kin, who resides at and whose post office address is 718 Springfield Avenue, Summit, New Jersey.



Elizabeth Frances Jones, a contingent remainderman of the trust, who resides at and whose post office address is 718 Springfield Avenue, Summit, New Jersey.

Dilys Demorest, a contingent remainderman of the trust, who resides at and whose post office address is Upper Dogwood Lane, Rye, New York.

William J. Demorest, Jr., a contingent remainderman of the trust, who resides at and whose post office address is Upper Dogwood Lane, Rye, New York.

Ann Demorest, a contingent remainderman of the trust, who resides at and whose post office address is [fol. 61] Upper Dogwood Lane, Rye, New York.

Carolyn Demorest, a contingent remainderman of trust, who resides at and whose post office address is Upper Dogwood Lane, Rye, New York.

There are no persons, other than those above named, interested in this proceeding.

All of the above persons are of full age and sound mind to the best of petitioner's knowledge, information and belief, except that William J. Demorest, Jr., and Ann Demorest are infants over the age of fourteen years, and Carolyn Demorest is an infant under the age of fourteen years. All of said infants reside with their mother, Wealthy Albro Lewis Demorest, who resides at and whose post office address is Upper Dogwood Lane, Rye, New York.

None of said infants has any general or testamentary guardian.

Wherefore, your petitioner prays:

I. That the account of its proceedings, as trustee under the last will and testament of Henry C. West, deceased, to and including the 31st day of July, 1940, be judicially settled and allowed.

II. That this Court determine the construction and effect of the "Fifth" clause of the Last Will and Testament of said Henry C. West, deceased, as to whether after the death of Zimri West, Emma M. West is entitled to the entire income from the trust created pursuant to said clause of said [fol. 62] last will and testament during her life or until she shall remarry.

III. That this Court construe the last will and testament of the said Henry C. West, deceased, for the purpose of determining what proportion, if any, of the moneys or property received or which may be received by way of rents or proceeds of sale of real property, acquired upon foreclosure or by deed in lieu of foreclosure of mortgages, or on account of claims based upon the guaranty of such mortgages, should be apportioned either to the income or principal of the trust estate created by said will and what part, if any, may or should be paid or applied to the use of those persons who now or hereafter may be entitled to receive or have applied to their use the income of said trust estate; and that your petitioner be instructed with respect to the proper method, under the true construction of said will, which should be employed in computing the net rents received from said or similar properties and the proper method of apportioning between principal and income such net rents, proceeds of sale of said properties or similar properties which may be hereafter acquired by your petitioner as such trustee, and of any moneys received or which may be received on account of any claims based upon such guaranties.

IV. That the persons above named may be cited to show cause why said account should not be judicially settled and allowed, why said last will and testament should not be judicially construed as prayed for in the petition herein, and why your petitioner should not be instructed and [fol. 63] directed by this Court as prayed for in the petition herein.

Dated: New York, N. Y., November 18, 1940.

City Bank Farmers Trust Company, by S. R. Walker,  
Trust Officer.

\* Attest: Crosby T. Smith, Asst. Secretary.

Mitchell, Taylor, Capron & Marsh, Attorneys for  
Petitioner, Office and Post Office Address: 20 Exchange Place, New York, N. Y.

(Verified by S. R. Walker, November 18, 1940.)

[fol. 64] IN SURROGATE'S COURT,  
County of New York.

EXCERPTS FROM INTERMEDIATE ACCOUNT OF TRUSTEE'S PROCEEDINGS AS ADJUSTED PURSUANT TO THE DECREE OF THE SURROGATE'S COURT

To the Surrogate's Court of the County of New York:

City Bank Farmers Trust Company hereby renders the following intermediate account of its proceedings as trustee under the last will and testament of Henry C. West, deceased, to and including the 31st day of July, 1940, and respectfully shows to this Court, upon information and belief:

[fol. 65] "Schedule A," hereto annexed, contains an itemized statement of all moneys and other property belonging to the estate or fund now accounted for which have come into [fol. 66] its hands or which have been received by any person for it or on its behalf as such trustee together with all accrued income or interest thereon which at the time of receipt by it constituted principal in its hands.

"Schedule AI," hereto annexed, contains a full and complete statement of all increases derived from capital assets whether due to sale, liquidation, distribution or for any other reason.

"Schedule AII", hereto annexed, contains a full and complete statement of all interest, dividends, rents and other income received by accountant, together with the date of each such receipt and the amount thereof.

"Schedule B", hereto annexed, contains a full and complete statement of all decreases in the value of capital assets, whether such assets are reported in Schedule "A" or in Schedule "G", together with a statement of the cause of each such decrease and whether the decrease has been actually realized and, if so, the date of realization and whether it arose by reason of sale, liquidation, distribution, physical loss, physical damage or any other reason.

[fol. 67] "Schedule C", hereto annexed, contains an itemized statement of all moneys chargeable to principal and paid by accountant for administration, funeral and other

necessary expenses together with the reason and object of each such expenditure and the date of each such payment.

"Schedule Ca", hereto annexed, contains a general statement of facts in connection with the acquisition of properties acquired upon foreclosure of mortgages held by accountant or by deed in lieu of foreclosure thereof. (See Schedules "Cb" to "Cj").

"Schedule Cb", hereto annexed, contains an itemized statement of all transactions since May 13, 1936 in connection with premises 46 Noll Street, Brooklyn, N. Y., acquired upon foreclosure; also a statement of facts in connection therewith and an apportionment of the net rents therefrom.

"Schedule Cc", hereto annexed, contains an itemized statement of all transactions since May 13, 1936 in connection with premises 1855 East 7th Street, Brooklyn, N. Y., acquired upon foreclosure; also a statement of facts in connection therewith and an apportionment of the net rents therefrom.

"Schedule Cd", hereto annexed, contains an itemized statement of all transactions since May 13, 1936 in connection with premises 2022 East 9th Street, Brooklyn, N. Y., acquired upon foreclosure; also a statement of facts in connection therewith and an apportionment of the net rents therefrom.

[fol. 68] "Schedule Ce", hereto annexed, contains an itemized statement of all transactions since May 13, 1936 in connection with premises 193 Bay 17th Street, Brooklyn, N. Y., acquired upon foreclosure; also a statement of facts in connection therewith and an apportionment of the net rents therefrom.

"Schedule Cf", hereto annexed, contains an itemized statement of all transactions since May 13, 1936 in connection with premises 1441-3 66th Street, Brooklyn, N. Y., acquired by deed in lieu of foreclosure; also a statement of facts in connection therewith and an apportionment of the net rents therefrom.

"Schedule Cg", hereto annexed, contains an itemized statement of all transactions since May 13, 1936 in con-

nection with premises 2047 East 27th Street, Brooklyn, N. Y., acquired by deed in lieu of foreclosure; also a statement of facts in connection therewith and an apportionment of the net rents therefrom.

"Schedule Ch", hereto annexed, contains an itemized statement of all transactions since May 13, 1936 in connection with premises 240 Floyd Street, Brooklyn, N. Y., acquired upon foreclosure; also a statement of facts in connection therewith and an apportionment of the net rents therefrom.

"Schedule Ci", hereto annexed, contains an itemized statement of all transactions in connection with premises 168 Morrison Avenue, West New Brighton, Staten Island, N. Y., acquired upon foreclosure; also a statement of facts in connection therewith and an apportionment of the net rents therefrom and proceeds of sale thereof.

[fol. 69] "Schedule Cj", hereto annexed, contains an itemized statement of all transactions in connection with premises 41 Montrose Avenue, Brooklyn, N. Y., acquired by deed in lieu of foreclosure; also a statement of facts in connection therewith and an apportionment of the net rents therefrom and proceeds of sale thereof.

[fols. 70-71] "Schedule H", hereto annexed, contains an itemized statement showing all property constituting capital and remaining in the hands of accountant, including a statement of all uncollected receivables and property rights due to the estate or fund as of the 31st day of July, 1940, the last day of this account.

"Schedule HI", hereto annexed, contains an itemized statement showing all property constituting undistributed income remaining in the hands of accountant including a statement of all uncollected receivables and property rights due to the estate or fund constituting income as of the 31st day of July, 1940, the last day of this account.



[fol. 72]

## SUMMARY

## AS TO PRINCIPAL

*Accountant charges itself as follows:*

With amount of all property originally received to constitute principal as shown in Schedule "A".....		\$132,753.26	
With amount of increases, as shown in Schedule "AI".....		10.50	
With amounts refunded to principal on account of advances (made by executor) for foreclosure expenses, etc. as follows:			
Premises 193 Bay 17th Street, Brooklyn, N. Y., as shown in Schedule "Ce" [page 103 herein]	\$29.16		
Premises 1441-3 66th Street, Brooklyn, N. Y., as shown in Schedule "Cf" [page 108 herein]	311.72	340.88	
			\$133,104.64

*Accountant credits itself as follows:*

With amount of decreases, as shown in Schedule "B".....	\$5,186.12		
With amount of payments for administration expenses, chargeable against principal, as shown in Schedule "C".....	766.76		
With amounts advanced (since May 13, 1936) from principal in connection with the following properties all situated in Brooklyn, N. Y., acquired by foreclosure or in lieu of foreclosure:			
Premises 46 Noll Street, as shown in Schedule "Cb" [page 88 herein]	\$751.68		
Premises 1855 East 7th Street, as shown in Schedule "Cc" [page 93 herein].....	420.98		
Premises 2022 East 9th Street, as shown in Schedule "Cd" [page 98 herein].....	2,315.53		
Premises 2047 East 27th Street, as shown in Schedule "Cg" [page 114 herein].....	147.48		
Premises 240 Floyd Street, as shown in Schedule "Ch" [page 119 herein].....	398.09	4,033.76	9,986.64
Leaving a balance of principal on hand of.....			\$123,118.00
consisting of the property set forth in Schedule "H", carried at inventory value of \$123,229.10, subject to a cash overdraft of \$155.70.			
			111.10

[fol. 73]

## AS TO INCOME

*Accountant charges itself as follows:*

With amount of all income received, as shown in Schedule "AII".....		\$28,921.89	
<i>Accountant credits itself as follows:</i>			
With amount of all payments for necessary expenses, including commissions, chargeable against income, as shown in Schedule "CII".....	\$1,154.99		
With amount of all payments to or for the account of beneficiaries from income, as shown in Schedule "FI".....	24,679.45	25,834.44	

Leaving a balance of income on hand of..... \$3,087.45  
 consisting of \$2,680.06 in cash and securities of \$407.39, as set forth in Schedule "HI".

The above balances are subject to the commissions of accountant estimated at \$1,356.81, as per Schedule "K", and the expenses of this accounting.

The attached schedules, which are severally signed by accountant, are part of this account.

Dated: New York, N. Y., July 31st, 1940.

CITY BANK FARMERS TRUST COMPANY  
By S. R. WALKER  
Trust Officer

Attest:

CROSBY T. SMITH  
Assistant Secretary.

MITCHELL, TAYLOR, CAPRON AND MARSH,  
Attorneys for Accountant,  
20 Exchange Place,  
New York, N. Y.

[fol. 74]

### SCHEDULE A

Value  
as appraised  
in New York  
Estate Tax  
Proceeding

1936

May 13

Received from Executor:

\$5,000. Bond and Mortgage, Ole O. Odegard and wife, covering property 168 Morrison Avenue, West New Brighton, Staten Island, New York, past due, interest at 6% payable June and December 1, guaranteed by Bond and Mortgage Guarantee Company (December 1, 1934 interest unpaid) In foreclosure	\$5,000 00
\$4,750. Bond and Mortgage, Joseph Cohen, covering property 41 Montrose Avenue, Brooklyn, past due, interest at 6% payable January and July 1, guaranteed by Bond and Mortgage Guarantee company (January 1, 1935 interest partially paid)	4,750 00

The following premises acquired by Executor by foreclosure of mortgages thereon held by decedent at date of his death, carried at the appraised value of said mortgages at date of death:

Premises 46 Noll Street, Brooklyn, New York	3,200 00
Premises 193 Bay 17th Street, Brooklyn, N. Y.	5,000 00
Premises 240 Floyd Street, Brooklyn, New York	2,700 00
Premises 1441-3 66th Street, Brooklyn, N. Y.	4,500 00
Premises 1855 East 7th Street, Brooklyn, New York	5,250 00
Premises 2022 East 9th Street, Brooklyn, New York	6,300 00
Premises 2047 East 27th Street, Brooklyn, New York	3,187 50

[fol. 75]

## SCHEDULE AI

PURCHASE MONEY MORTGAGE, CARMINE MARRONE,  
COVERING 41 MONTROSE AVENUE, BROOKLYN

Increase

1939			
Dec. 18	Payment in reduction of principal	\$50.00	
1940			
Apr. 8	do	50.00	
June 20	do	50.00	
		<u>\$150.00</u>	
	Inventory value reduced	\$150.00	

[fol. 76]

## SCHEDULE AII

BOND AND MORTGAGE, JOSEPH COHEN, COVERING  
41 MONTROSE AVENUE, BROOKLYN

1936				
June 15	Balance of interest on \$4,750. at 6% due January 1, 1935	\$16.49		
15	On account interest on \$4,750. due July 1, 1935	\$13.51		
June 20	Payment on account of interest due July 1, 1935	7.23		
29	do	25.00		
July 28	do	55.00		
Aug. 25	Balance at 6%	41.76	142.50	
25	On account of interest due January 1, 1936	\$3.24		
Nov. 18	do	55.00		
19	do	8.00	76.24	\$235.23

PURCHASE MONEY MORTGAGE, CARMINE MARRONE,  
COVERING 41 MONTROSE AVENUE, BROOKLYN

1939				
Nov. 16	3 months interest on \$3,200. at 5% to November 9, 1939	\$40.00		
1940				
Apr. 8	3 months interest on \$3,150. at 5% to February 9, 1939	39.38		
	Interest on \$50. payment to December 18, 1939	28		
June 20	3 months interest on \$3,100. at 5% to May 9, 1939	38.75		
	Interest on \$50. payment to April 8	41		118.82

[fol. 77]

**PREMISES 168 MORRISON AVENUE, WEST NEW  
BRIGHTON, STATEN ISLAND, NEW YORK (ACQUIRED  
BY FORECLOSURE SEE SCHEDULE C1)**

1938

Aug. 25 Share of proceeds of sale allocated to income, per Schedule C1 ..... 714 44

**PREMISES 41 MONTROSE AVENUE, BROOKLYN, NEW  
YORK (ACQUIRED BY FORECLOSURE SEE SCHEDULE C1)**

1939

Aug. 9 Share of proceeds sale allocated to income, consisting of \$407.39 undivided interest (subject to a preferred interest of principal of \$1,023.51) in \$3,200. purchase money mortgage, Carmine Marrone, covering said premises, due August 9, 1944, interest at 5% payable February 9th quarterly, see Schedule Cj ..... 407 39

**NET RENTS UP TO 3% PER ANNUM ON PROPERTIES  
ACQUIRED BY FORECLOSURE:**

Premises 46 Noll Street, Brooklyn, New York, per Schedule Cb .....	\$207 61	
Premises 1855 East 7th Street, Brooklyn, New York, per Schedule Cc .....	630 00	
Premises 193 Bay 17th Street, Brooklyn, New York, per Schedule Ce .....	358 67	
Premises 1441-3 66th Street, Brooklyn, New York, per Schedule Cf .....	527 04	
Premises 2047 East 27th Street, Brooklyn, New York, per Schedule Cg .....	310 59	
Premises 240 Floyd Street, Brooklyn, New York, per Schedule Ch .....	134 43	2,168 34
		<u>\$28,921 89</u>

[fol. 78]

**SCHEDULE B**

1938

Aug. 25 Net share of proceeds of premises 168 Morrison Avenue, West New Brighton, Staten Island, New York, apportioned to principal, as per Schedule C1 (in addition to reimbursement for advances) ..... \$2,812 78

Value of mortgage Ole O. Odegaard and wife (foreclosed per Schedule C1) as per Schedule "A" ..... 5,000 00 \$2,187 22

1939

Aug. 9 Net share of proceeds of premises 41 Montrose Avenue, Brooklyn, New York, apportioned to principal, as per Schedule Cj, (in addition to reimbursement for advances) ..... \$1,769 10

Value of mortgage Joseph Cohen (foreclosed per Schedule Cj) as per Schedule "A" ..... 4,750 00 2,980 90

Containing a General Statement of Facts in Connection With the Acquisition of Properties Acquired Upon Foreclosure of Mortgages Held by Accountant or by Deed in Lieu of Foreclosure Thereof. (See Schedules Cb to Cj)

As is set forth in Schedule A of the account of City Bank Farmers Trust Company, of its proceedings as executor of the last will and testament of Henry C. West, deceased to May 15, 1935 heretofore filed in this Court on or about the 17th day of June, 1935, in a proceeding brought by your accountant as such executor for the judicial settlement of its accounts as such, the estate of Henry C. West consisted in part of the following described bonds and mortgages:

- \$5,000. Bond and Mortgage of Ole O. Odegaard and Wife, covering property of 168 Morrison Avenue, West New Brighton, Staten Island, New York, due December 19, 1933, interest  $5\frac{1}{2}\%$  payable June and December 1, valued in said account at 100,
- \$7,000. Bond and Mortgage, Minnie Appel and Husband, covering property 1855 East 7th Street, Brooklyn, New York, due January 17, 1935, interest at  $5\frac{1}{2}\%$  payable June and December 1, valued in said account at 75,
- \$5,000. Bond and Mortgage, Maria Capcorosso, covering property 193 Bay 17th Street, Brooklyn, New York, due June 3, 1934, interest at  $5\frac{1}{2}\%$  payable May and November 1, valued in said account at 100,
- \$4,000. Bond and Mortgage, Mary A. O'Neill, covering property 46 Noll Street, Brooklyn, New York, due February 17, 1935, interest at  $5\frac{1}{2}\%$  payable May and November 1, valued in said account at 80,
- \$4,750. Bond and Mortgage, Joseph Cohen, covering property 41 Montrose Avenue, Brooklyn, New York, due October 2, 1933, interest at  $5\frac{1}{2}\%$  payable January and July 1, valued in said account at 100,



\$3,000. Bond and Mortgage, Morris Pakulski, et ano, covering property 240 Floyd Street, Brooklyn, New York, due September 27, 1933, interest at 4% payable January and July 1, valued in said account at 90,

\$4,250. Bond and Mortgage, Well-Bilt Building Corporation, covering property 2047 East 27th Street, Brooklyn, New York, due November 1, 1935, interest at 5½% payable May and November 1, valued in said account at 75,

\$7,000. Bond and Mortgage, Charles Pollacek, covering property 2022 East 9th Street, Brooklyn, New York, due April 17, 1934, interest at 6% payable January, April, July and October 1, valued in said account at 90,

\$4,500. Bond and Mortgage, Gaetano Loffredo and Maria Loffredo, covering property 1441/3 66th Street, Brooklyn, New York, due April 20, 1933, interest at 5½% payable June and December 1, valued in said account at 100.

As is set forth in Schedule CII of said account and in Schedules C-a and F of the supplemental account of City Bank Farmers Trust Company of its proceedings as said executor from May 15, 1935 to May 13, 1936 filed in said proceeding on or about the 29th day of June, 1936, and as further set forth herein, the properties covered by the aforementioned bonds and mortgages have been acquired by your accountant upon foreclosure or by deed in lieu of foreclosure.

The decree of this Court duly made and entered on the 10th day of August, 1936, judicially settling and allowing the account and supplemental account of proceedings of City Bank Farmers Trust Company, as executor as aforesaid, duly made and entered in this Court on the 10th day of August, 1936, provided in part as follows:

[fol. 81] "Further Ordered, Adjudged and Decreed that each of the properties received as a result of foreclosure and transferred by said executor to itself as trustee under said decedent's will, be held in a separate account by the trustee, wherein all expenses and disbursements incurred in connection with the acquisition

of each property as shown in the account and supplemental account herein, together with any and all future receipts and disbursements in connection with each property, so that the same may be taken into consideration by the trustee in apportioning the proceeds received upon the ultimate sale of the respective properties between principal and income and that the rights of all persons interested in said trust be and the same hereby are reserved to assert upon any future accounting that any such receipts and disbursements whether made prior or subsequent to this accounting should be taken into consideration by the court in determining the proper apportionment of the proceeds of sale of said properties;"

Your accountant has managed these properties, received the rents therefrom, paid the operating and other expenses in connection therewith. Said receipts and disbursements since May 13, 1936 are hereinafter set forth in Schedules Cb to Cj, inclusive, together with a restatement, in so far as your accountant is advised is necessary for present purposes, of the receipts and disbursements prior to May 13, 1936, which were set forth in said account and supplemental account of your accountant as executor as aforesaid. Two of the properties so acquired, to wit, premises 168 Morrison Avenue, West New Brighton, Staten Island, New York, and 41 Montrose Avenue, Brooklyn, New York, have been sold by your accountant.

In Schedules Cb to Cj, inclusive, your accountant has set forth an apportionment of the income from such properties as have not been sold and of the income and proceeds of sale of such properties as have been sold in the manner your accountant is advised is proper under the laws of this State, and your accountant requests that the respective rights of the income beneficiaries and the remaindermen in such income and proceeds of sale be determined by the decree to be entered herein.

[fol. 82] As indicated above, each of said mortgages was guaranteed by Bond and Mortgage Guarantee Company. On the 2nd day of August, 1933, an order was entered in the Supreme Court of the State of New York, County of Kings, placing the company in rehabilitation and directing the Superintendent of Insurance of the State of New York to take possession thereof. Thereafter and on or about

the 31st day of December, 1937, an order was entered in the Supreme Court of the State of New York, Kings County, placing said company in liquidation, directing the Superintendent of Insurance of the State of New York to take possession of the property of said Bond and Mortgage Guarantee Company and further directing that the final date for the presentation of claims by certificate holders and creditors of said company should be the 30th day of September, 1938.

Your accountant accordingly filed with the said liquidator proofs of claim in connection with the guaranty of the aforesaid mortgages, and said claims have been allowed in varying amounts as is hereinafter set forth. Your accountant is informed and believes that the claims will not be paid in full but that from time to time dividends thereupon will be paid. Your accountant requests that the decree to be entered herein determine the respective rights of the income beneficiaries and the remaindermen in the amounts which may be so received and that your accountant be instructed by said decree accordingly.

City Bank Farmers Trust Company, by S. R. Walker,  
Trust Officer.

[fols. 83-84]

#### SCHEDULE Cb

46 Noll Street, Brooklyn, N. Y.

The bond and mortgage on the above premises was in the principal amount of \$4,000, bearing interest at the rate of 6% per annum and netting to the decedent and his estate 5½% per annum after the deduction of the one-half of one per cent charge of Bond and Mortgage Guarantee Company. The agency of this company was terminated pursuant to letter of your accountant dated July 20, 1934.

The owner having defaulted in the payment of the principal of the obligation, interest thereon from November 1, 1933 and taxes on the real property, your accountant brought an action in the Supreme Court of Kings County to foreclose the mortgage upon the premises. The property was bid in by your accountant at the foreclosure sale and was conveyed to your accountant by a Referee's deed made and delivered February 26, 1935.

The premises consist of a plot 25 feet by 100 feet in size and are improved by a three-story and cellar frame building containing two four-room apartments on each floor. The tenants of the apartments are required to furnish their own heat and hot water. At the date of the acquisition of the property it was vacant except for one apartment occupied by a janitor. Your accountant endeavored to sell the same but has been unable to do so and has been required to operate the property in the meantime. Your accountant was required to make extensive repairs in order to put the premises in a tenantable condition and in order to comply with orders of the Tenement House Department concerning the condition of the property.

Your accountant has filed proof of claim dated July 22, 1938, in connection with the guaranty of this mortgage, with the Superintendent of Insurance, as Liquidator of the Bond and Mortgage Guarantee Company. This claim was [fols. 85-86] in the amount of \$7,680.59, and \* \* \* was allowed in the amount of \$3,680.59.

STATEMENT SUMMARIZING THE RENTS, CARRYING CHARGES, CAPITAL IMPROVEMENTS,  
COSTS OF ACQUIRING TITLE, ETC., BY FISCAL YEARS, FROM THE DATE OF ACQUISITION  
OF SAID PREMISES, AND A CALCULATION OF THE AMOUNT OF NET  
RENTS PAYABLE TO-INCOME ACCOUNT

I	II	III	IV	V	VI	VII	VIII	IX
Period	Gross Rents	Carrying Charges	Net Rents	Net Deficit	Amount of Net Rents Transferred to Income (up to 3% of \$4,000 face of mortgage)	Excess over 3%	Capital Improvements and Charges	Costs of Acquisition of Premises (foreclosure expenses and charges)
<i>Fiscal year ending 2/25/36</i>								
Per 1st account.....		\$188 63					\$717 37	\$1,411 97
Per Supp. account.....		214 19						
Sub totals.....		\$402 82		\$402 82			\$717 37	\$1,411 97
<i>Fiscal year ending 2/25/37</i>								
Per Supp. account.....	\$16 00	175 63					60	
Per this account.....	345 00	209 71					238 40	
Sub totals.....	\$361 00	\$464 34		\$103 34			\$167 00	
<i>Fiscal year ending 2/25/38</i>								
Per Supp. account.....	614 00	526 39	\$87 61		\$87 61		40 00	
<i>Fiscal year ending 2/25/39</i>								
Per Supp. account.....	737 00	854 48		117 48			525 00	
<i>Fiscal year ending 2/25/40</i>								
Per Supp. account.....	843 00	679 09	163 91		120 00	\$43 91		
Period to 7/31/40.....	284 00	236 99	47 01		undetermined (see note)	undetermined (see note)	10 00	
Totals.....	\$2,839 00	\$3,162 17	\$298 53	\$623 61	\$207 61	\$43 91	\$1,459 37	\$1,411 97



[fol. 88]

STATEMENT SUMMARIZING THE AMOUNTS ADVANCED TO DATE FROM PRINCIPAL  
IN CONNECTION WITH SAID PROPERTY

Expenses of acquisition of title (foreclosure expenses and payments of liens on property at date of acquisition), per column IX	\$1,411.97
Capital improvements and charges per column VIII	1,459.37
Operating deficits per column V	623.64
	<b>\$3,494.98</b>
Less amount of net rents in excess of 3% per annum per column VII	43.91
Net sum advanced by principal to date	<b>\$3,451.07</b>
Consisting of amounts advanced:	
Per Schedule "CII" of 1st account	\$1,600.60
Per Schedule "Ca" of Supplemental account	1,098.79
During this accounting period	751.68
	<b>\$3,451.07</b>

NOTE: There remains a balance of cash in this account of \$47.01 consisting of net rents the allocation of which is not determinable until the end of the current fiscal year.

[fols. 89-90]

## SCHEDULE Cc

1855 East 7th Street, Brooklyn, N. Y.

The bond and mortgage on the above premises was in the principal amount of \$7,000, bearing interest at the rate of 6% per annum and netting to the decedent and his estate

5½% per annum after the deduction of the one-half of one per cent charge of the Bond and Mortgage Guarantee Company. The agency of this company was terminated pursuant to letter of your accountant dated July 27, 1934.

The owner of the property having defaulted in the payment of the principal of the obligation; interest thereon from June 1, 1932, and taxes on the real property, your accountant brought an action in the Supreme Court, Kings County, to foreclose the mortgage upon the premises. The property was bid in by your accountant at the foreclosure sale and was conveyed to your accountant by a Referee's deed made and delivered September 24, 1935.

Your accountant is informed and believes that the Bond and Mortgage Guarantee Company advanced to the decedent the installment of interest due December 1, 1932, pursuant to the terms of the guaranty.

The premises consist of a plot of ground approximately 33 feet by 120 feet in size and are improved by a one and

one-half story and cellar frame and stucco private dwelling containing eight rooms and two baths and by a garage at the rear of the plot: At the date of the acquisition of the property it was occupied by a tenant holding under a lease executed by the holder of the second mortgage upon the property. This tenant remained on the premises under leases from your accountant until March 30, 1939. Your accountant has endeavored to sell the property but has been unable to do so and in the meantime has operated the same.

Your accountant has filed proof of claim dated July 22, 1938, in connection with the guaranty of this mortgage, with the Superintendent of Insurance, as Liquidator of the Bond and Mortgage Guarantee Company. This claim was in the amount of \$10,292.36 and . . .

[fol. 91] was allowed in the amount of \$3,294.03.

STATEMENT SUMMARIZING THE RENTS, CARRYING CHARGES, CAPITAL IMPROVEMENTS,  
COSTS OF ACQUIRING TITLE, ETC., BY FISCAL YEARS, FROM THE DATE OF ACQUISITION  
OF SAID PREMISES, AND A CALCULATION OF THE AMOUNT OF NET  
RENTS PAYABLE TO INCOME ACCOUNT

I	II	III	IV	V	VI	VII	VIII	IX
Period	Gross Rents	Carrying Charges	Net Rents	Net Deficit	Amount of Net Rents Transferred to Income (up to 3% of \$7,000 face of mortgage)	Excess over 3%	Capital Improvements and Charges	Costs of Acquisition of Premises (foreclosure expenses and charges)
<i>Fiscal year ending 9/23/36</i>								
Per 1st account and supp. account	\$330.00	\$283.23					\$69.71	\$2,044.89
Per this account	290.00	14.50						(219.24)
Sub totals	\$620.00	\$297.73	\$322.27	—	\$210.00	\$112.27	\$69.71	\$1,825.65
<i>Fiscal year ending 9/23/37</i>	700.00	335.65	364.35	—	210.00	154.35	35.36	
<i>Fiscal year ending 9/23/38</i>	747.58	522.27	225.31	—	210.00	15.31	19.46	
<i>Fiscal year ending 9/23/39</i>	325.33	1,029.87	—	\$704.54	—	—	18.58	
<i>Period to 7/31/40</i>	636.67	415.59	221.08	—	Undetermined (see note)	Undetermined (see note)	97.44	
Totals	\$3,029.58	\$2,601.11	\$1,133.01	\$704.54	\$630.00	\$281.93	\$240.55	\$1,825.65

[Note: Figures in parentheses is credit.]

[fol. 93]

**STATEMENT SUMMARIZING THE AMOUNTS ADVANCED TO DATE FROM PRINCIPAL  
IN CONNECTION WITH SAID PROPERTY**

Expenses of acquisition of title (foreclosure expenses and payments of liens on property at date of acquisition), per column IX	\$1,825.65
Capital improvements and charges, per column VIII	240.55
Operating deficits, per column V	704.54
	\$2,770.74
Less amount of net rents in excess of 3% per annum, per column VII	281.93
Net sum advanced by principal to date	<u>\$2,488.81</u>
Consisting of amounts advanced:	
Per Schedule "C" of 1st account	\$100.00
Per Schedule "Ca" of Supplemental account	1,967.83
During this accounting period	420.98
	<u>\$2,488.81</u>

NOTE: There remains a balance of cash in this account of \$221.08 consisting of net rents the allocation of which is not determinable until the end of the current fiscal year.

[fol. 94]

**SCHEDULE Cd**

2022 East 9th Street, Brooklyn, N. Y.

The bond and mortgage on the above premises was in the principal amount of \$7,000, bearing interest at the rate of 6% per annum and netting to the decedent and his estate  $5\frac{1}{2}\%$  per annum after the deduction of the one-half of one per cent charge of the Bond and Mortgage Guarantee Company. The agency of this company was terminated pursuant to letter of your accountant dated September 12, 1934.

The owner having defaulted in the payment of the principal obligation, interest thereon from April 1, 1934 and taxes on the real property your accountant brought an action in the Supreme Court, Kings County, to foreclose the mortgage upon the premises. The property was bid in by your accountant at the foreclosure sale and was conveyed to your accountant by a Referee's deed made and delivered October 1, 1935.

The premises consist of a plot of ground 60 feet by 100 feet in size and are improved by a two and one-half story frame detached private dwelling containing ten rooms and bath, and by a garage at the rear of the plot. At the date of the acquisition of the property it was vacant. Your accountant has been unable to sell the property and has endeavored to secure a tenant for the same but has been

unable to do so to the date of this account. Your accountant installed a caretaker in the premises on June 1, 1936 in order to protect the same against depreciation.

Your accountant has filed proof of claim dated July 22, 1938, in connection with the guaranty of this mortgage, with the Superintendent of Insurance, as Liquidator of the Bond and Mortgage Guarantee Company. This claim was in the amount of \$11,093.16 and . . .

[fols. 95-96] was allowed in the amount of \$5,593.16.



STATEMENT SUMMARIZING THE RENTS, CARRYING CHARGES, CAPITAL IMPROVEMENTS,  
COSTS OF ACQUIRING TITLE, ETC., BY FISCAL YEARS, FROM THE DATE OF ACQUISITION  
OF SAID PREMISES, AND A CALCULATION OF THE AMOUNT OF NET  
RENTS PAYABLE TO INCOME ACCOUNT

I	II	III	IV	V	VI	VII	VIII	IX
Period	Gross Rents	Carrying Charges	Net Rents	Net Deficit	Amount of Net Rents Transferred to Income (up to 3% of \$7,000 face of mortgage)	Excess over 3%	Capital Improvements and Charges	Costs of Acquisition of Premises (foreclosure expenses and charges)
<i>Fiscal year ending 9/30/36</i>								
Per Supp. account	—	\$345.59					\$3.47	\$1,578.07
Per this account	—	18.89					76.91	
Sub totals	—	\$372.48	—	\$372.48	—	—	\$72.38	\$1,578.07
<i>Fiscal year ending 9/30/37</i>								
<i>Fiscal year ending 9/30/38</i>	—	494.89	—	494.89	—	—	15.00	
<i>Fiscal year ending 9/30/39</i>	\$25.00	539.70	—	539.70	—	—	—	
<i>Period to 7/31/40</i>	45.00	638.44	—	613.44	—	—	—	
		589.70	—	544.70	—	—	12.00	
Totals	\$70.00	\$2,635.21	—	\$2,565.21	—	—	\$99.38	\$1,578.07

[fol. 98]

**STATEMENT SUMMARIZING THE AMOUNTS ADVANCED TO DATE FROM PRINCIPAL  
IN CONNECTION WITH SAID PROPERTY.**

Expenses of acquisition of title (foreclosure expenses and payments of liens on property at date of acquisition), per column IX	\$1,578.07
Capital improvements and charges, per column VIII	99.88
Operating deficits, per column V	2,565.21
Net sum advanced by principal to date	<u>\$4,242.66</u>
Consisting of amounts advanced:	
Per Schedule "Ca" of Supplemental account	\$1,927.13
During this accounting period	2,315.53
	<u>\$4,242.66</u>

[fol. 99]

**SCHEDULE Ce**

193 Bay 17th Street, Brooklyn, N. Y.

The bond and mortgage on the above premises was in the principal amount of \$5,000, bearing interest at the rate of 6% per annum and netting to the decedent and his estate 5½% per annum after the deduction of the one-half of 1% charge of Bond and Mortgage Guarantee Company. The agency of this company was terminated pursuant to letter of your accountant dated January 23, 1935.

The owner having defaulted in the payment of the principal obligation, interest thereon from May 1, 1934, and taxes upon the real property, your accountant brought an action in the Supreme Court, Kings County, to foreclose the mortgage upon the premises. The property was bid in by your accountant at the foreclosure sale and was conveyed to your accountant by Referee's deed made and delivered September 16, 1935.

The premises consist of an irregular plot of ground having a frontage of 48.6 feet and a depth of about 96 feet and are improved by a two-story and cellar, frame, stucco covered, detached private dwelling containing seven rooms and bath. At the date of the acquisition of the property it was occupied by the former owner but shortly thereafter was vacated by him. Your accountant was required to spend substantial sums in rehabilitating the property in order that a tenant might be secured and was successful in securing a tenant in the spring of 1936. Your accountant has endeav-

ored to sell the property but has been unable to do so, and has operated the same to the date of this account.

Your accountant has filed proof of claim dated July 22, 1938 in connection with the guaranty of this mortgage in the proceeding for the liquidation of Bond and Mortgage Guarantee Company. This claim was in the amount of [fols. 100-101] \$7,319.18 and . . . was allowed in the sum of \$1,119.18.

[fol. 102]

STATEMENT SUMMARIZING THE RENTS, CARRYING CHARGES, CAPITAL IMPROVEMENTS,  
COSTS OF ACQUIRING TITLE, ETC., BY FISCAL YEARS, FROM THE DATE OF ACQUI-  
TION OF SAID PREMISES, AND A CALCULATION OF THE AMOUNT OF NET  
RENTS PAYABLE TO INCOME ACCOUNT

I	II	III	IV	V	VI	VII	VIII	IX
Period	Gross Rents	Carrying Charges	Net Rents	Net Deficit	Amount of Net Rents Transferred to Income (up to 3% of face of mortgage)	Excess over 3%	Capital Improve-ments and Charges	Costs of Acquisition of Premises (foreclosure expenses and charges)
<i>Fiscal year ending 9/15/36</i>								
Per Supp. account.....	\$85.00	\$285.68					\$343.81	\$1,021.38
Per this account.....	160.00	8.00						
Sub totals.....	\$245.00	\$293.68	—	\$48.68	—	—	\$343.81	\$1,021.38
<i>Fiscal year ending 9/15/37</i>								
.....	480.00	352.80	\$127.20	—	\$127.20	—	15.00	
<i>Fiscal year ending 9/15/38</i>								
.....	400.42	318.95	81.47	—	81.47	—	—	
<i>Fiscal year ending 9/15/39</i>								
.....	481.41	304.25	177.16	—	150.00	\$27.16	—	
<i>Period to 7/31/40</i>								
.....	482.16	312.69	169.47	—	Undetermined (see note)	Undetermined (see note)	135.00	
Totals.....	\$2,088.99	\$1,582.37	\$555.30	\$48.68	\$358.67	\$27.16	\$493.81	\$1,021.38

[fol. 103]

STATEMENT SUMMARIZING THE AMOUNTS ADVANCED TO DATE FROM PRINCIPAL  
IN CONNECTION WITH SAID PROPERTY

Expenses of acquisition of title (foreclosure expenses and payments of liens on property at date of acquisition), per column IX.....	\$1,021.38
Capital improvements and charges, per column VIII.....	493.81
Operating deficit, per column V.....	48.68
	<hr/>
	\$1,563.87
Less amount of net rents in excess of 3% per annum, per column VII.....	27.16
	<hr/>
Net sum advanced by principal to date.....	\$1,536.71
Consisting of amounts advanced:	
Per Schedule "Ca" of Supplemental account.....	\$1,565.87
Refunded during this accounting period.....	29.16
	<hr/>
	\$1,536.71

NOTE: There remains a balance of cash in this account of \$169.47 consisting of net rents, the allocation of which is not determinable until the end of the current fiscal year.

[fol. 104]

SCHEDULE Cf

1441-3 66th Street, Brooklyn, N. Y.

The bond and mortgage on the above premises was in the principal amount of \$4,500, bearing interest at the rate of 6% per annum, netting to the decedent and his estate 5½% per annum after the deduction of one-half of 1% charge of the Bond and Mortgage Guarantee Company. The agency of this company was terminated pursuant to letter of your accountant dated June 25, 1935.

The owner defaulted in the payment of the principal obligation, the interest thereon from December 1, 1934 and taxes on the real property, and your accountant as executor accepted a deed to the premises from the then owners of the premises in lieu of foreclosure, which deed was made and delivered November 8, 1935.

The premises consist of a plot of ground 43 x 100 feet in size and are improved by a three-story and cellar, brick building consisting of one store on the first floor with an apartment of four rooms, two three-room apartments on the second floor and one six-room apartment on the third floor and by a one-car frame garage in the rear of the apartment. The tenants of the apartments are required to furnish their own heat and hot water.



At the date of the acquisition of the property, the premises were fully occupied, but within a few weeks thereafter the two tenants of the second floor apartments vacated. Your accountant was required to make extensive repairs in order that the premises might be placed in a tenantable condition and in order to comply with an order of the Tenement House Department concerning the condition of the property. Your accountant has been unable to sell the premises and in the meantime has operated the same.

Your accountant filed proof of claim, dated July 22, 1938, in connection with the guaranty of this mortgage in the proceeding for the Liquidation of Bond and Mortgage Guarantee Company. This claim was in the amount of \$6,132.58, and . . .

[fols. 105-106] was allowed in the amount of \$532.59.

STATEMENT SUMMARIZING THE RENTS, CARRYING CHARGES, CAPITAL IMPROVEMENTS,  
COSTS OF ACQUIRING TITLE, ETC., BY FISCAL YEARS, FROM THE DATE OF ACQUISITION  
OF SAID PREMISES, AND A CALCULATION OF THE AMOUNT OF NET  
RENTS PAYABLE TO INCOME ACCOUNT

I	II	III	IV	V	VI	VII	VIII	IX
Period	Gross Rents	Carrying Charges	Net Rents	Net Deficit	Amount of Net Rents Transferred to Income (up to 3% of \$4,500 face of mortgage)	Excess over 3%	Capital Improvements and Charges	Costs of Acquisition of Premises (foreclosure expenses and charges)
<i>Fiscal year ending Nov. 7, 1936</i>								
Per Supp. Account	\$293 00	\$296 36					\$472 22	\$734 05
Per this Account	480 50	167 25					83 00	
Sub totals	\$773 50	\$551 36	\$222 14	—	\$135 00	\$87 14	\$167 47	\$734 05
<i>Fiscal year ending Nov. 7, 1937</i>	740 50	618 46	122 04	—	122 04	—	—	
<i>Fiscal year ending Nov. 7, 1938</i>	1,032 02	732 80	279 22	—	135 00	144 22	—	
<i>Fiscal year ending Nov. 7, 1939</i>	864 06	652 81	211 25	—	135 00	76 25	4 00	
<i>Period to July 31, 1940</i>	649 77	337 60	312 17	—	Undetermined (see note)	Undetermined (see note)	—	
Totals	\$4,059 85	\$2,913 03	\$1,146 82	—	\$527 04	\$307 61	\$471 47	\$734 05

[fol. 108]

STATEMENT SUMMARIZING THE AMOUNTS ADVANCED TO DATE FROM PRINCIPAL  
IN CONNECTION WITH SAID PROPERTY

Expenses of acquisition of title (expenses in lieu of foreclosure and payments of liens on property at date of acquisition), per column IX .....	\$734.05
Capital improvements and charges, per column VIII .....	471.47
	<u>1,205.52</u>
Less amount of net rents in excess of 3% per annum, per column VII .....	307.61
Net sum advanced by principal to date .....	<u>\$897.91</u>
Consisting of amounts advanced:	
Per Schedule "Ca" of Supplemental Account .....	\$1,209.63
Refunded during this accounting period .....	311.72
	<u>\$897.91</u>
NOTE: There remains a balance of cash in this account of consisting of net rents, the allocation of which is not determinable until the end of the current fiscal year.	<u>\$312.17</u>

[fols. 109-110]

SCHEDULE Cg

2047 East 27th Street, Brooklyn, N. Y.

The bond and mortgage on the above premises was in the principal amount of \$4,250, bearing interest at the rate of 6% per annum, and netting to the decedent and his estate  $5\frac{1}{2}\%$  per annum after the deduction of the one-half of one per cent. charge of Bond and Mortgage Guarantee Company. The agency of this company was terminated pursuant to letter of your accountant dated August 8, 1934.

The owner having defaulted in the payment of the principal obligation, interest thereon from November 1, 1932, and taxes on the real property, your accountant authorized the institution of an action to foreclose the mortgage upon the premises, but the same was not pressed to conclusion since upon the offer of the owner the property was acquired by your accountant by deed in lieu of foreclosure made and delivered January 22, 1936.

The premises consist of a plot of ground 18.9 feet by 100 feet in size and are improved by a two-story and cellar, brick attached private dwelling containing six rooms and bath. At the date of the acquisition of the property it was vacant, but shortly thereafter a tenant was secured. Your accountant has endeavored to sell the property, but has

been unable to do so and, in the meantime, has operated the same.

Your accountant has filed proof of claim dated July 22nd, 1938, in connection with the guaranty of this mortgage in the proceeding for the liquidation of Bond and Mortgage Guarantee Company. The claim was in the amount of [fols. 111-112] \$7,293.25, and . . . was allowed in the sum of \$3,293.25.

[fol. 113]

STATEMENT SUMMARIZING THE RENTS, CARRYING CHARGES, CAPITAL IMPROVEMENTS,  
COSTS OF ACQUIRING TITLE, ETC., BY FISCAL YEARS, FROM THE DATE OF ACQUISITION  
OF SAID PREMISES, AND A CALCULATION OF THE AMOUNT OF NET  
RENTS PAYABLE TO INCOME ACCOUNT

I	II	III	IV	V	VI	VII	VIII	IX
Period	Gross Rents	Carrying Charges	Net Rents	Net Deficit	Amount of Net Rents Transferred to Income (up to 3% of \$4,250 face of mortgage)	Excess over 3%	Capital Improvements and Charges	Costs of Acquisition of Premises (payments in lieu of foreclosure and charges)
<i>Fiscal year ending 1/31/37</i>								
Per Supp. account.....	\$90.00	\$114.58					\$137.02	\$1,605.23
Per this account.....	405.00	129.69					207.54	
<b>Sub totals.....</b>	<b>\$495.00</b>	<b>\$253.27</b>	<b>\$241.73</b>	—	<b>\$127.50</b>	<b>\$114.23</b>	<b>\$335.56</b>	<b>\$1,605.23</b>
<i>Fiscal year ending 1/21/38</i> .....	467.50	401.58	65.92	—	65.92	—	168.78	
<i>Fiscal year ending 1/21/39</i> .....	437.50	347.51	89.99	—	89.99	—	(81.03)	
<i>Fiscal year ending 1/21/40</i> .....	606.88	579.70	27.18	—	27.18	—	—	
<i>Period to 7/31/40</i> .....	150.00	105.74	44.26	—	Undetermined (see note)	Undetermined (see note)	—	
<b>Totals.....</b>	<b>\$2,156.88</b>	<b>\$1,687.80</b>	<b>\$469.08</b>	—	<b>\$310.59</b>	<b>\$114.23</b>	<b>\$423.31</b>	<b>\$1,605.23</b>

[NOTE: Figure in parentheses is credit.]

[ol. 114]

STATEMENT SUMMARIZING THE AMOUNTS ADVANCED TO DATE FROM PRINCIPAL  
IN CONNECTION WITH SAID PROPERTY

Expenses of acquisition of title (expenses in lieu of foreclosure and payments of liens on property at date of acquisition), per column LX:	\$1,605.23
Capital improvements and charges, per column VIII:	423.81
	<u>\$2,028.54</u>
Less amount of net rents in excess of 3% per annum, per column VII:	114.23
	<u>\$1,914.31</u>
Consisting of amounts advanced:	
Per Schedule "Ca" of Supplemental account:	\$1,766.83
During this accounting period:	147.48
	<u>\$1,914.31</u>
NOTE: There remains a balance of cash in this account of consisting of net rents, the allocation of which is not determinable until the end of the current fiscal year.	<u>\$44.26</u>

[fol. 115]

## SCHEDULE Ch

240 Floyd Street, Brooklyn, N. Y.

The bond and mortgage on the above premises was in the principal amount of \$3,000, bearing interest at the rate of 6% per annum and netting to the decedent and his estate 5½% per annum after the deduction of the one-half of one per cent. charge of Bond and Mortgage Guarantee Company. The agency of this company was terminated pursuant to letter of your accountant dated July 5, 1934.

The owner of the property encountered difficulties in maintaining the property and paying interest upon the mortgage and it was agreed by means of a letter dated October 22, 1934, with the then owner of the property that the interest rate might be reduced to 4% per annum. Interest at this rate was paid to July 1, 1935. For the owner's default in payment of the principal obligation and interest thereon from July 1, 1935, and taxes on the real property, your accountant commenced an action in the Supreme Court, Kings County, to foreclose the mortgage upon the premises. The property was bid in by your accountant at the foreclosure sale and was conveyed to your accountant by a Referee's deed made and delivered May 8, 1936.



The premises consist of a plot of ground 25 feet by 100 feet in size and are improved by a three-story and cellar, frame apartment building containing one apartment of four rooms and bath on each of the first and second floors and one of five rooms and bath on the third floor. The tenants of the apartments are required to furnish their own heat and hot water.

Your accountant has been unable to sell the premises and in the meantime has operated the same. At the date of acquisition the premises were fully occupied, all of the tenants continuing as such.

Your accountant has filed proof of claim dated July 22, 1938, in connection with the guaranty of this mortgage, with the Superintendent of Insurance, as Liquidator of the Bond and Mortgage Guarantee Company. This claim was in the [fols. 116-117] amount of \$4,553.42 and \* \* \* was allowed in the amount of \$1,553.42.

[col. 118]

STATEMENT SUMMARIZING THE RENTS, CARRYING CHARGES, CAPITAL IMPROVEMENTS,  
COSTS OF ACQUIRING TITLE, ETC., BY FISCAL YEARS, FROM THE DATE OF ACQUISITION  
OF SAID PREMISES, AND A CALCULATION OF THE AMOUNT OF NET  
RENTS PAYABLE TO INCOME ACCOUNT

I	II	III	IV	V	VI	VII	VIII	IX
Period	Gross Rents	Carrying Charges	Net Rents	Net Deficit	Amount of Net Rents Transferred to Income (up to 3% of \$3,000 face of mortgage)	Excess over 3%	Capital Improvements and Charges	Costs of Acquisition of Premises (foreclosure expenses and charges)
Fiscal year ending 5/7/37	\$492.00	\$475.46	\$16.54	—	\$16.54	—	\$288.52	\$849.79
Fiscal year ending 5/7/38	494.50	425.70	68.80	—	68.80	—	74.50	
Fiscal year ending 5/7/39	554.00	555.07	—	\$1.07	—	—	29.00	
Fiscal year ending 5/7/40	490.04	440.95	49.09	—	49.09	—	5.00	
Period to 7/31/40	127.50	28.05	99.45	—	Undetermined (see note)	Undetermined (see note)	—	
Totals	\$2,158.04	\$1,925.23	\$233.83	\$1.07	\$134.43	—	\$397.02	\$849.79

[fol. 119]

STATEMENT SUMMARIZING THE AMOUNTS ADVANCED TO DATE FROM PRINCIPAL  
IN CONNECTION WITH SAID PROPERTY

Expenses of acquisition of title (foreclosure expenses and payments of liens on property at date of acquisition), per column IX	\$849.79
Capital improvements and charges, column VIII	397.02
Operating deficit, per column V	1.07

\$1,247.88

Consisting of amounts advanced per Schedule "Ca" of supplemental account	\$849.79
During this accounting period	398.09

\$1,247.88

NOTE: There remains a balance of cash in this account of consisting of net rents, the allocation of which is not determinable until the end of the current fiscal year. \$99.45

[fols. 120-121]

SCHEDULE C

168 Morrison Avenue, West New Brighton, Staten Island,  
N. Y.

The bond and mortgage on the above premises was in the principal amount of \$5,000. bearing interest at the rate of 6% per annum, netting to the decedent and his estate 5½% per annum after the deduction of the one-half of one per cent. charge of Bond and Mortgage Guarantee Company. The agency of this company was terminated pursuant to letter of your accountant dated October 16, 1934.

The owner having defaulted in the payment of the principal of the obligation, interest thereon from June 1, 1934, and taxes upon the real property, your accountant brought an action in the Supreme Court, Richmond County, to foreclose the mortgage upon the premises. The property was bid in by your accountant at the foreclosure sale and was conveyed to your accountant by a referee's deed made and delivered March 5, 1937.

The premises consist of a plot of ground 35 feet by 100 feet in size and are improved by a 2½ story and cellar, frame and stucco, one-family detached dwelling, containing seven rooms, bath and porch and by a frame one-car garage.

At the date of the acquisition of the property it was occupied by a tenant at a rental of \$40. a month. The rental was subsequently increased to the sum of \$45. a month. In the spring of 1937, substantial exterior painting and repairs

and decoration of the interior were undertaken, in order that the property might be preserved and its appearance improved for purposes of sale. The property was sold and conveyed on August 25, 1939, for a consideration of \$4,500. payable entirely in cash.

Your accountant filed a proof of claim in connection with the guaranty of this mortgage, dated July 22, 1938, in the proceeding for the liquidation of Bond and Mortgage Guarantee Company. This claim was in the amount of \$6,691.18 and . . . .

[fol. 122] after negotiation, was allowed in the amount of \$1,691.18.

# RECAPITULATION

I	II	III	IV	V	VI
Period	Gross Rents	Carrying Charges	Net Rents	Capital Improvements and Charges	Costs of acquisition (foreclosure expenses and charges on property)
Fiscal year ending 3/4/38.....	\$470.00	\$237.70	\$232.30	\$367.80	\$604.07
Period from 3/5/38 to date of sale 8/25/38.	270.70	162.83	107.87	4.08	
	<u>\$740.70</u>	<u>\$400.53</u>	<u>\$340.17</u>	<u>\$371.88</u>	<u>\$604.07</u>

[fol. 123]

## STATEMENT SHOWING THE NET PROCEEDS OF SALE OF SAID PROPERTY:

1938

Aug. 1	Received from Louis P. Orlemann initial payment on account of purchase price	\$500.00
26	Received from Amy Orlemann balance of purchase price	4,000.00
		<u>\$4,500.00</u>

Less the following expenses in connection with sale:

1938

Sept. 12	Paid Cornelius G. Kolff, Inc., broker's commission	\$225.00
12	Paid Mitchell, Taylor, Capron & Marsh, attorneys' services and disbursements re sale	112.00
		<u>337.00</u>

Net proceeds of sale..... \$4,163.00

**STATEMENT OF APPORTIONMENT, BETWEEN PRINCIPAL AND INCOME OF THE  
NET SUM REALIZED FROM SAID PROPERTY:**

Net proceeds of sale as above .....		\$4,163.00
Less reimbursement of principal advances:		
Foreclosure expenses and charges, Column VI .....	\$604.07	
Capital improvements and charges, Column V .....	371.88	
	<u>\$975.95</u>	
Less net rents, Column IV .....	340.17	635.78
Net sum to be apportioned .....		<u>\$3,527.22</u>
Face amount of foreclosed mortgage .....	\$5,000.00	
Interest thereon at 6% from June 1, 1934 (date to which interest was paid) to August 25, 1938, date of sale .....	1,270.00	
	<u>\$6,270.00</u>	
Principal is entitled to 5,000/6,270 of \$3,527.22 or .....		\$2,812.78
(transferred to Schedule "B" of account)		
Income is entitled to 1,270/6,270 of \$3,527.22 or .....		714.44
(transferred to Schedule "AII" of account)		<u>\$3,527.22</u>

[fol. 124]

**SCHEDULE Cj**

41 Montrose Avenue, Brooklyn, N. Y.

The bond and mortgage on the above premises was in the principal amount of \$4,750. bearing interest at the rate of 6%, netting to the decedent and his estate  $5\frac{1}{2}\%$  per annum after the deduction of the one-half of one per cent. charge of Bond and Mortgage Guarantee Company. The agency of this Company was terminated pursuant to letter of your accountant dated August 8, 1934.

Your accountant instituted an action to foreclose the mortgage upon the premises by a summons and complaint dated November 24, 1934, in which action an order was entered appointing a receiver of the property. This action was not, however, pressed to judgment and the property was acquired on December 23, 1936, by deed in lieu of foreclosure, from Leonarda Godino, the then owner of the premises, the receiver in the meantime having accounted and been discharged.

The premises consist of a plot of ground 25 feet by 100 feet in size and are improved by a three-story and cellar, frame building, consisting of two stores on the first floor and two apartments each on the second and third floors.

The tenants of such apartments were required to furnish their own heat and hot water.

At the date of the acquisition of the property, interest from July 1, 1935 was unpaid, except for \$76.24 paid on account thereof.

At the date of the acquisition of the property, one of the stores was rented, one apartment was occupied by the owner and two of the other apartments were rented. Within a short time, however, one of these tenants vacated. Your accountant endeavored to sell the property, operating the same in the meanwhile and making extensive repairs to the property in order to comply with orders of the Tenement House Department and to place the property in a tenable condition.

The property was sold and conveyed on August 9, 1939, for a consideration of \$4,000. made up of cash in the amount of \$800. and a purchase money bond and mortgage maturing in five years in the amount of \$3,200. with interest [fols. 125-126] payable quarterly at the rate of 5% per annum and amortization payments of \$50. to be made on each interest date. At the date of this account, interest on said purchase money mortgage was paid to May 9th, 1940, and \$150. had been paid in amortization.

Your accountant has filed a proof of claim dated July 22, 1938 in connection with the guaranty of this mortgage in the proceeding for the liquidation of Bond and Mortgage Guarantee Company. This claim was in the amount of \$6,725.56 and . . . was allowed in the amount of \$2,725.56.

[fol. 127]

#### RECAPITULATION

I	II	III	IV	V	VI
Period	Gross Rents	Carrying Charges	Net Rents	Capital Improvements and Charges	Costs of acquisition (in lieu of foreclosure)
Fiscal year ending 12/22/37	\$254.00	\$472.65	(\$218.65)	\$998.09	\$265.43
Fiscal year ending 12/22/38	759.00	522.83	136.17	319.25	
Period to 8/9/39 date of sale	483.20	325.86	157.34	-0-	
	<u>\$1,496.20</u>	<u>\$1,421.34</u>	<u>\$74.86</u>	<u>\$1,317.34</u>	<u>\$265.43</u>

[Note: Figures in parentheses are deficits.]



## STATEMENT SHOWING THE NET PROCEEDS OF SALE OF SAID PROPERTY:

1939

Aug. 7	Received from Carmine Mar- rone initial payment on pur- chase price.....		\$300.00
17	Received from Carmine Mar- rone balance of purchase price as follows: Purchase money mortgage in- terest at 5% payable quar- terly with \$50. quarterly amortization, balance prin- cipal due August 9, 1944..	\$3,200.00	
	Cash.....	500.00	3,700.00
			<u>\$4,000.00</u>
	Less the following expenses of sale:		
17	Paid Herbert Zarnikauer, brok- er's commission.....	\$200.00	
17	Paid Mitchell, Taylor, Capron & Marsh, attorneys' services and disbursements re sale...	115.60	315.60
			<u>\$3,684.40</u>
	Net proceeds of sale.....		

[fol. 128]

STATEMENT OF APPORTIONMENT BETWEEN PRINCIPAL AND INCOME, OF THE  
NET SUM REALIZED FROM SAID PROPERTY:

## Net proceeds of sale as above:

Purchase money mortgage.....	\$3,200.00	
Cash.....	484.40	\$3,684.40
Less reimbursement of principal advances:		
Costs of acquisition, etc., Column VI.....	\$265.43	
Capital improvements, etc., Column V.....	1,317.34	
	<u>\$1,582.77</u>	
Less net rents, Column IV.....	74.86	1,507.91
		<u>\$2,176.49</u>

Net sum to be apportioned consisting of \$3,200. purchase  
money mortgage in which principal has a prior interest  
of \$1,023.51 in reimbursement of advances

Face amount of foreclosed mortgage.....	\$4,750.00	
Interest thereon at 6% from July 1, 1935 to August 9, 1939.....	\$1,170.08	
Less paid on account.....	76.24	1,093.84
		<u>\$5,843.84</u>

Interest in  
Purchase money  
mortgage subject  
to prior interest

Principal is entitled to 4,750/5,843.84ths of \$2,176.49 or (Transferred to Schedule "B" of account)	\$1,769.10
Income is entitled to 1,093.84/5,843.84ths of \$2,176.49 or (transferred to Schedule "AII" of account)	407.39

\$2,176.49

[fol. 129]

## SCHEDULE H

In setting forth inventory values of the items listed below, accountant is not to be understood as representing that the inventory value set opposite any of the items below represents the market value of such item. Your accountant is of the opinion that at least in some instances the market value is less than the inventory value.

	<i>Inventory Value</i>
\$4,375. Home Owners Loan Corporation, Series "M", 1½% due June 1, 1947-45, at cost	\$4,480.27
\$5,300. United States Treasury, 2½% due September 15, 1952-50, at cost	5,538.72
\$3,000. Bond and Mortgage, Realty Sales Company, covering property 1138 East 2nd Street, Brooklyn, New York, past due, interest at 6% payable May and November 1, guaranteed by Bond and Mortgage Guarantee Company	3,000.00
\$4,750. Bond and Mortgage, Ida Sommer and husband, covering property 85 West End Avenue, Brooklyn, New York, past due, interest at 5% payable March 1st quarterly, guaranteed by Bond and Mortgage Guarantee Company	4,750.00
\$4,250. Bond and Mortgage, Novodoff Construction Company Inc., covering property 4510 Avenue "L", Brooklyn, New York, past due, interest at 6% payable February 1st quarterly	4,250.00
\$5,100. Bond and Mortgage, Luigi Principe and wife, covering property 193 Skillman Street, Brooklyn, New York, past due, interest at 5½% payable January 1st quarterly, guaranteed by Bond and Mortgage Guarantee Company	5,100.00
\$4,650. Bond and Mortgage, Esther Rascofsky and husband, covering property 318-20 Williams Avenue, Brooklyn, New York, past due, interest at 5% payable May and November 1st, guaranteed by Bond and Mortgage Guarantee Company, inventory value	4,100.00
[fol. 130]	
\$6,000. Bond and Mortgage, Elizabeth Ennis, covering property 2109 Dean Street, Brooklyn, New York, past due, interest at 4% payable March 1st quarterly, guaranteed by Bond and Mortgage Guarantee Company	6,000.00
\$12,500. Bond and Mortgage, Isidore Herleth and wife, covering property 88 Nassau Street and 211 Pearl Street, Brooklyn, New York, past due, interest at 6% payable June and December 1st, guaranteed by Bond and Mortgage Guarantee Company	12,500.00
\$4,750. Bond and Mortgage, Dickel Construction Company, covering property 8630-78th Street, Woodhaven, Long Island, past due, interest at 6% payable January and July 1st, guaranteed by Bond and Mortgage Guarantee Company	4,750.00
\$4,250. Bond and Mortgage, John W. McGrath, covering property 502 Hancock Street, Brooklyn, New York, past due, interest at 6% payable January and July 1st, guaranteed by Bond and Mortgage Guarantee Company	4,250.00
\$8,000. Bond and Mortgage, 95th Street Building Corporation, covering property 1102 Winthrop Street, Brooklyn, New York, past due, interest at 5% payable May and November 1, guaranteed by Bond and Mortgage Guarantee Company	8,000.00
\$7,000. Bond and Mortgage, Thomas W. Lewis, covering property 10 West Drive, Plandome, Hempstead, Long Island, past due, interest at 6% payable January 1st quarterly, guaranteed by Bond and Mortgage Guarantee Company	7,000.00
\$3,950. Bond and Mortgage, Saider and Mary Tolkochoff, covering property 400 Wythe Avenue, Brooklyn, New York, past due, interest at 5% payable February 1st quarterly, guaranteed by Bond and Mortgage Guarantee Company	3,950.00
\$3,280. Bond and Mortgage, Glenn H. Frost and Mary E. Frost, covering property 1202 Avenue "N", Brooklyn, New York, past due, interest at 6% June and December 1st, guaranteed by Bond and Mortgage Guarantee Company	3,280.00

Inventory  
Value

\$9,500. Bond and Mortgage, Josephine Curtis and husband, covering property 139 Wood Lane, Woodmere, Long Island, past due, interest at 6% payable June and December 1st, guaranteed by Bond and Mortgage Guarantee Company	9,500.00
With respect to the above bonds and mortgages which are noted to be guaranteed by the Bond and Mortgage Guarantee Company accountant has filed proofs of claim in the proceeding for the liquidation of said company. The status of such claims is set forth in Schedule "L".	
[fol. 131]	
\$2,642.61 undivided interest (of which \$873.51 is a preferred interest) in \$3,050. purchase money bond and mortgage, Carmine Marrone, covering 41 Montrose Avenue, Brooklyn, New York, due August 9, 1944, interest at 5% payable February 9th quarterly	2,642.61
The following premises acquired by foreclosure of mortgages thereon held by decedent at date of his death, carried at the appraised value of said mortgages at date of death.	
In these premises income also has an interest which will be determined only when said premises are sold. See Schedule Cb to Ch inclusive for status of claims allowed with respect to the guaranty of mortgages in connection with which such premises were acquired:	
Premises 46 Noll Street, Brooklyn, New York (on which there has been advanced by principal a total of \$3,451.07) see Schedule Cb	3,200.00
Premises 193 Bay 17th Street, Brooklyn, New York (on which there has been advanced by principal a total of \$1,536.71) see Schedule Ce	5,000.00
Premises 240 Floyd Street, Brooklyn, New York (on which there has been advanced by principal a total of \$1,247.88) see Schedule Ch	2,700.00
Premises 1441-3 66th Street, Brooklyn, New York (on which there has been advanced by principal a total of \$897.91) see Schedule Cf	4,500.00
Premises 1855 East 7th Street, Brooklyn, New York (on which there has been advanced by principal a total of \$2,488.81) see Schedule Cc	5,250.00
Premises 2022 East 9th Street, Brooklyn, New York (on which there has been advanced by principal a total of \$4,242.66) see Schedule Cd	6,300.00
Premises 2047 East 27th Street, Brooklyn, New York (on which there has been advanced by principal a total of \$1,914.31) see Schedule Cg	3,187.50
	\$123,229.10
Less cash overdraft	111.10
	\$123,118.00

[fol. 132]

NOTE: In addition to the above property capital has an interest (which cannot be determined until the close of the respective current fiscal years) in the net rents on hand on July 31, 1940 in the following accounts for properties acquired by foreclosure:

	<i>Net Rents to 7/31/40</i>
Premises 46 Noll Street, Brooklyn, see Schedule Cb.....	\$47.01
Premises 1855 East 7th Street, Brooklyn, see Schedule Ce.....	221.08
Premises 193 Bay 17th Street, Brooklyn, see Schedule Ce.....	169.47
Premises 1441-3 66th Street, Brooklyn, see Schedule Cf.....	312.17
Premises 2047 East 27th Street, Brooklyn, see Schedule Cg.....	44.26
Premises 240 Floyd Street, Brooklyn, see Schedule Ch.....	99.45
	<u>\$893.44</u>

[fol. 133]

## SCHEDULE HI

\$407.39 undivided interest (subject to a preferred interest of principal of \$873.51) in \$3,050.00 purchase money bond and mortgage, Carmine Marrone, covering 41 Montrose Avenue, Brooklyn, New York, due August 9, 1944, interest at 5% payable February 9th, quarterly:

Cash.....	\$407.39
	<u>2,680.06</u>
	\$3,087.45

NOTE: In addition to the above property income has an interest (which cannot be determined until the close of the respective current fiscal years) in the net rents on hand on July 31, 1940 in the following accounts for properties acquired by foreclosure:

	<i>Net Rents to 7/31/40</i>
Premises 46 Noll Street, Brooklyn, see Schedule Cb.....	\$47.01
Premises 1855 East 7th Street, Brooklyn, see Schedule Ce.....	221.08
Premises 193 Bay 17th Street, Brooklyn, see Schedule Ce.....	169.47
Premises 1441-3 66th Street, Brooklyn, see Schedule Cf.....	312.17
Premises 2047 East 27th Street, Brooklyn, see Schedule Cg.....	44.26
Premises 240 Floyd Street, Brooklyn, see Schedule Ch.....	99.45
	<u>\$893.44</u>

NOTE: When the above mentioned premises and 2022 East 9th Street are sold income will be entitled to a share of the proceeds, the amount of which cannot be determined until such sale.

[NOTE: Figures in italics are the adjustments made by paragraphs 8 to 14 of the decree herein.]

[Affidavit of S. R. Walker, Trust Officer of the accountant verifying account sworn to on November 18, 1940.]

[fol. 134] IN SURROGATE'S COURT,  
County of New York.

REPORT OF SPECIAL GUARDIAN AND OBJECTIONS TO CONSTITUTIONALITY OF SECTION 17-C OF THE PERSONAL PROPERTY LAW  
AND OTHER OBJECTIONS

To the Surrogate's Court of the County of New York:

Gerald P. Culkin, as Special Guardian of William J. Demorest, Jr., an infant over the age of fourteen years, Ann Demorest, an infant over the age of fourteen years, and Carolyn Demorest, an infant under the age of fourteen years, respectfully submits the following:

That I am a counselor at law; that since my appointment as Special Guardian herein, I have to the best of my ability made myself acquainted with the rights of my wards and that I have taken all the steps necessary for the protection of such rights to the best of my knowledge and as I believe; that I have filed with the Clerk of the Court a duly acknowledged consent and an affidavit of qualification and thereafter entered upon the performance of my duties as such Special Guardian.

I have examined all the papers on file in the office of the Clerk of this court in the within proceeding.

This proceeding brought by a trustee of a decedent's estate, in addition to seeking a judicial settlement of its intermediate account, asks for instructions on several matters. At the outset I desire to request permission to file a [fol. 135] supplemental report which will deal with those items not herein considered. I believe that several of the matters discussed in this report are sufficiently unique to render advisable the confinement of this report and the consideration of the court to those matters alone.

The petition quotes paragraph "Fifth" of the Will and asks instruction from the court as to what disposition shall be made of the monthly allowance of \$100 out of net income payable to the brother of testator. Said brother has died. I believe that it was the testator's intention that after the death of his brother the entire net income be paid to the widow of the testator.

The petitioner requests this court to construe the Last Will and Testament of the deceased for the purpose of

determining what proportion, if any, of the moneys or property received or which may be received by way of rents or proceeds of sale of real property acquired by the foreclosure or by deed in lieu of foreclosure of mortgages or on account of claim based upon the guarantee of such mortgages, should be apportioned either to the income or principal of the trust estate; and what part, if any, may or should be paid or applied to the use of those persons who now or hereafter may be entitled to receive or have applied to their use the income of said trust estate; and with respect to the proper method, under the construction of said will which should be employed in computing the net rents received from said properties and the apportionment thereof between principal and income.

Without extensive preliminary discussion I state these general questions involved herein:

[fol. 136] 1. Is Subsection 2 of Section 17-c of the Personal Property Law constitutional in all respects?

2. Whether Subsection 2 of Section 17-c of the Personal Property Law is or is not constitutional, partly or wholly, are certain disbursements made by the trustee and shown in the account, capital charges or carrying charges, so as to determine net income and the 3% of net income directed to be paid the income beneficiary by Section 17-c of the Personal Property Law if said section is applied?

It is my opinion that Subsection 2 of Section 17-c is unconstitutional in its entirety.

Regardless of the general objection contained in the next preceding paragraph hereof, subsection 2 of Section 17-c is unconstitutional in so far as said subsection attempts to be retroactive in its application, in so far as its application results in an allocation of income by a series of annual periods commencing with the anniversary date of acquisition of title regardless of the fact that there might not exist any true net income, to the detriment of the trust principal; and in so far as it fixes an arbitrary rate of income to the income beneficiary to the detriment of the trust principal.

Having arrived at the foregoing conclusions, I therefore find it necessary to interpose the following objection to the account.



I. I object to the following items as having been allocated to the income beneficiary by the application of Section 17-c:

[fol. 137] Schedule Cb-15—\$207.61—46 Noll St. Brooklyn, N. Y.

Schedule Ce-11—\$630.00—1855 East 7th St., Brooklyn, N. Y.

Schedule Ce-11—\$358.67—193 Bay 17th St. Brooklyn, N. Y.

Schedule Cf-15—\$527.04—1441-3 66th St., Brooklyn, N. Y.

Schedule Cg-12—\$340.19—2047 East 27th St., Brooklyn, N. Y.

Schedule Ch-14—\$149.43—240 Floyd St., Brooklyn, N. Y., and to Schedule AII at page 13 and Schedule III at page 1 in so far as said schedules reflect the allocation and transfer of said items to income.

II. I object to the following items of income presently in the hands of the trustees constituting income of the current fiscal year, being reserved by the trustee for allocation through the application of Section 17-c:

Schedule Cb-16—\$47.01—46 Noll St., Brooklyn, N. Y.

Schedule Ce-12—\$221.08—1855 East 7th St., Brooklyn, N. Y.

Schedule Ce-12—\$169.47—193 Bay 17th St., Brooklyn, N. Y.

Schedule Cf-16—\$312.17—1441-3 66th St., Brooklyn, N. Y.

Schedule Cg-13—\$44.26—2047 East 27th St., Brooklyn, N. Y.

[fol. 138] Schedule Ch-15—\$99.45—240 Floyd St., Brooklyn, N. Y., and to Schedule III in so far as a similar notation with respect to said items is therein set forth.

The two preceding objections to such allocation and contemplated allocation are made on the ground that they are contrary to law for the reasons:

1. Subsection 2 of Section 17-c of the Personal Property Law is not properly applicable and should not be construed to be applicable to trusts created and in existence prior to April 13, 1940, the effective date of said statute.

2. Subsection 2 of Section 17-c of the Personal Property Law is not properly applicable and should not be construed to be applicable to mortgages acquired by such a trustee prior to said April 13, 1940, the effective date of said statute.

3. Subsection 2 of Section 17-c of the Personal Property Law is not properly applicable and should not be construed to be applicable to real property acquired by such trustee prior to April 13, 1940, the effective date of said statute, by the foreclosure of a mortgage theretofore held by such trustee on said real property or by deed in lieu of such foreclosure.

4. Section 17-c of the Personal Property Law is not properly applicable and should not be construed to be applicable to any income from real property which was acquired by [fol. 139] such trustee prior to April 13, 1940, the effective date of said statute.

5. Section 17-c of the Personal Property Law is not properly applicable and should not be construed to be applicable to any rents or income received from such real property prior to April 13, 1940, the effective date of said statute.

6. Section 17-c of the Personal Property Law is not properly applicable and should not be construed to be applicable to any rents or income received from such real property since or subsequent to April 13, 1940, the effective date of said statute.

To the extent that it is attempted to apply said Section 17-c to any of the foregoing subjects set forth in subparagraphs 1 to 6 and to the properties received by the accountant, said statute is invalid and unconstitutional and its provisions arbitrary and said statute deprives my wards as residuary remaindermen of the trust estate of property without due process of law and in a manner prohibitive by and contrary to the provisions of Section 6, Article I of the Constitution of the State of New York and to the provisions of the 14th Amendment to the Constitution of the United States of America.

It is my contention and I therefore respectfully submit to the court that the sums hereinbefore referred to should be and are properly applicable and should therefore be used in reduction of the amounts advanced from the principal of the trust estate in accordance with the equitable rules established by the decisions of the courts of this State prior to [fol. 140] the enactment of Section 17-c of the Personal Property Law, and certainly to the repayment to principal of advances made out of principal for expenditures properly chargeable against income.

III. I object to the allocation to income of the sums hereinbefore mentioned to the extent that said sums exceed net profit, if any, derived from the operation of the respective real properties from the date of the acquisition thereof to the close of the last complete fiscal year of the operation of said properties, that is to say, I specifically object to

Schedule	Property	Gross rents to said date	Carrying charges to said date	Net Profit	Sum allocated to income per account	Excess of sum allocated over net profit if any
Cb	46 Noll St., Brooklyn, N. Y.	\$2,555.00	\$2,848.12	*\$293.13	\$207.61	\$207.61
Ce	1855 E. 7th St., Brooklyn, N. Y.	2,392.91	2,185.52	207.39	630.00	422.61
Ce	193 Bay 17th, Brooklyn, N. Y.	1,606.83	1,269.68	337.15	358.67	21.52
Ch	240 Floyd St., Brooklyn, N. Y.	2,030.54	1,882.18	148.36	149.43	1.07
	* Deficit					

The last mentioned objection numbered "III" is made on the ground that, to the extent the sums so allocated to income, exceed the net profits from the operation of the respective properties during such period such allocation is contrary to law, in that said sums do not constitute the net income within the purview, meaning and intent of subdivision 2 of said Section 17-c of the Personal Property Law and it is my contention that said sums should be used to [fol. 141] the extent of such excess in reduction of the amounts advanced from principal in connection with the operation of the respective premises; and I object to the statement contained in Schedule Cb of said Account at page 16 and to a similar statement in Schedule H 1 to the effect that a part of the sum of \$47.01 hereinbefore mentioned of rents from 46 Noll Street, Brooklyn, New York, received during the current fiscal year may constitute income and

this objection is based on the ground that such a statement and the action contemplated thereby are erroneous in and contrary to law; that all of said sum will necessarily be required to repay principal advances for deficits resulting from the operation of said property prior to the commencement of said current fiscal year and no part of said sum of \$47.01 can constitute net income.

IV. I object to the statement of apportionment between principal and income of the proceeds of sale of premises 168 Morrison Avenue, West New Brighton, Staten Island, New York (Schedule Ci, pages 8 and 9) in that the accountant improperly computes the interest of income in said proceeds of sale at the rate of 6% per annum from June 1, 1934, the date to which interest was paid, to August 25, 1938, the date of sale. The mortgage foreclosed was a guaranteed mortgage. Although the interest rate reserved in the mortgage was 6%, the guarantee provides for the payment of  $\frac{1}{2}\%$  to the guarantor corporation for servicing the said mortgage and the purchaser of said guaranteed mortgage did not anticipate or expect to receive as income from said [fol. 142] mortgage any rate of interest above  $5\frac{1}{2}\%$ . To apply this objection specifically to the account, I object to the item in Schedule AII at page 12 under date August 25, 1938 which fixes the share of the proceeds of sale properly allocated to income per schedule Ci at \$714.44 and to the item of Schedule III, in so far as the amount shown therein to be income consists of cash incorrectly allocated to income, pursuant to the aforesaid improper computation. This objection is made on the ground that said apportionment is erroneous and that as hereinbefore stated, the interest of the income account in said proceeds of sale should be computed at the rate of  $5\frac{1}{2}\%$  per annum from June 1, 1934 to August 25, 1938, which was the interest rate actually received by and anticipated by the purchaser of the guaranteed mortgage, in which event the computation would be as follows:

Face amount of foreclosed mortgage	\$5,000.00
Interest thereon at $5\frac{1}{2}\%$ from June 1, 1934 (date to which interest was paid) to August 25, 1938 (date of sale)	1,164.17
	<hr/>
	\$6,164.17

Principal is entitled to 500000/616417ths of \$3,-	
527.22, or	\$2,861.07
Income is entitled to 116417/616417ths of \$3,527.-	
22, or	666.15
	<hr/>
	\$3,527.22

In any event, should the court deem my suggested allocation at  $5\frac{1}{2}\%$  not to be properly applicable to the entire period from June 1, 1934 to August 25, 1938, the interest of the income account in said proceeds of sale should be com-[fol. 143] puted at said  $5\frac{1}{2}\%$  per annum, at least from June 1, 1934 to October 16, 1934 when, as shown by the account, the agency of the guarantor corporation was terminated and at 6% thereafter to August 25, 1938, the date of sale. In the event this method of computation is applied the figures would be as follows:

Face amount of foreclosed mortgage	\$5,000.00
Interest thereon at $5\frac{1}{2}\%$ from June 1, 1934 (date to which interest was paid) to October 16, 1934 (date when agency of guaranty company was terminated) and at 6% from October 17, 1934 to August 25, 1938 (date of sale)	\$1,260.62
	<hr/>
	\$6,260.62
Principal is entitled to 500000/626062nds of \$3,-	
527.22, or	\$2,816.99
Income is entitled to 126062/626062nds of \$3,527.-	
22, or	710.23
	<hr/>
	\$3,527.22

V. I make the same objection to the apportionment between principal and income of the sum realized upon the sale of premises 41 Montrose Avenue, Brooklyn, New York, substituting the applicable date to which interest was last paid, the date of acquisition and the date of sale effecting premises 41 Montrose Avenue, Brooklyn, New York. Applying said objection specifically to the account, I object to the following item in Schedule AII at page 12, which reads as follows:

Premises 41 Montrose Avenue, Brooklyn, New York (acquired by foreclosure; see Schedule Cj)

[fol. 144] Aug. 9, 1939 Share of proceeds of sale allocated to income, consisting of \$407.39 undivided interest (subject to a preferred interest of principal of \$1,023.51) in \$3,200.00 purchase money mortgage, Carmine Marrone, covering said premises, due August 9, 1944, interest at 5% payable February 9th quarterly, see Schedule Cj \$407.39

and to the reflected item in Schedule III to the extent that the interest in the purchase money mortgage therein referred to and shown as income consists in such interest in said mortgage incorrectly allocated to income pursuant to the foregoing computation, which I maintain is improper. This objection is on the ground that such apportionment is erroneous, that the interest allocated to income in said proceeds of sale should be computed at the rate of  $5\frac{1}{2}\%$  per annum from July 1, 1935 to August 9, 1939, in which event the computation would be as follows:

Face amount of foreclosed mortgage \$4,750.00

Interest thereon at  $5\frac{1}{2}\%$

from July 1, 1935 to August 9, 1939 (date of sale) \$1,072.74

Less interest paid on account 76.24 996.50

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\$5,746.50

Principal is entitled to 475000/574650ths of \$2,176.49, interest in purchase money mortgage subject to prior interest, or

\$1,799.07

Income is entitled to 99650/574650ths of \$2,176.49, interest in purchase money mortgage subject to prior interest, or

377.42

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\$2,176.49

[fol. 145] In passing and for the reason that hereafter it may become important with respect to other properties which may be foreclosed by the trustee or taken in lieu of foreclosure, I call attention to the mortgage affecting premises 240 Floyd Street, Brooklyn, N. Y. and referred to in Schedule CH-1 et seq. The court will note (Schedule Ch at page 1) the trustee agreed by letter to the owner of



the mortgaged premises, that the interest rate be reduced to 4%. Accordingly this was the interest rate when the property was foreclosed and this is the rate which should be used in estimating income's claim preliminary to allocation. It would prove helpful if the Surrogate were to instruct on this matter also.

VI. I object to the charge as capital improvements in said account of items of expense more specifically set forth in Schedule A hereto annexed and made a part hereof. This objection is predicated on the following grounds:

1. That said expenditures do not constitute capital expenses and were not made for capital improvements and that neither under the provisions of Section 17-c of the Personal Property Law, nor under the law as it existed prior to the enactment of said section and regardless of the constitutionality or effectiveness of said section, the items of expenditure do not constitute capital charges.

2. Said expenditures are ordinary expenses connected with the continuance of the property in substantially its existing state and are payable from income. They are properly chargeable and should be charged against rents received from the respective premises and should be considered and deducted from gross income in arriving at the net income of the respective premises.

VII. Applying the objection numbered "VI" to the income presently in the hands of the accountant and derived during the current fiscal year, I object to the statements contained in the account that the rents received during the current fiscal years can or might be allocable to income at the end of the respective fiscal years of said properties to the extent that said sums consist of rents which would be necessary to restore principal for the advances made in connection with the items contained in Schedule A hereto annexed because, as set forth in objection "VI", said items accruing during the said fiscal years would be improperly charged to capital and as capital improvements and are properly chargeable to and should be deducted from gross rents of the respective properties in determining the net income of said properties.

As to the disposition of any sums which may hereafter be received by the trustee on general claims allowed by the

Superintendent of Insurance as Liquidator of the Guarantor companies I respectfully report as follows:

According to the information received by me through activities of my office in similar matters, the likelihood of distribution on general claims is very remote. The amounts of such claims are determined as the difference between the value of the security and the debt due on the guaranty as of the effective date of the order of liquidation. If any sums [fol. 147] are received on these claims they should be apportioned between principal and interest as they appeared on the effective date of the order of liquidation.

I need not go into a lengthy discussion of the law of allocation of income and proceeds of sale as determined by the cases antedating enactment of Section 17-c. I believe all parties concerned in this proceeding and the Court will concede that said section is designed to change, or modify, the law as fixed and applied in those cases.

Getting down to the case at bar—if this proceeding had been concluded in March, 1940 the decree would have undoubtedly followed the law as stated in *Matter of Chapal*, 269 N. Y. 464 and in *Matter of Otis*, 276 N. Y. 101 and cases therein cited with approval. Presumably in March, 1940 the residuary remainder would have had adjudged to it certain property rights which, because this proceeding was instituted after April, 1940, are not property rights if Section 17-c, subsection 2, is applied retroactively. Why should the rights of a person in the application of income during the years 1938, 1937, 1936, 1935 fixed by decree dated March, 1940 differ from rights of similarly situated persons for the same period because the rights in the latter instance are adjudicated by decree dated May, 1940 or later? The application of Section 17-c to the property rights of the remaindermen prior to the enactment of the Statute amounts to a deprivation of property without due process of law.

The Statute presumes to legislate intent. It is not reasonable to presume that a testator intended to prefer the life [fol. 148] beneficiary in every instance over the remainderman. Let us suppose testator had devised the property in fee to the widow, could we also presume that he expected or intended application of the general estate to the support of the property when it was in trouble? In fact, were testator alive would he not consider disbursements out of his reserve funds ordinarily deducted from gross income as prop-

erly payable back to reserve before he considered any income as being real income and regardless of yearly income and disbursements? It should not be argued that the only effect of subsection 2 of Section 17-c is to postpone the repayment to principal until the sale. There can be no assurance that the property will bring enough on the sale to produce an equitable result. There might be sound argument for the Statute if the real net income were progressively allocated between principal and income in proportion as on a sale but there is no justification of the arbitrary preference of 3% of the mortgage principal to the income beneficiary in advance.

The will sets up the status of principal and income. These two accounts, although "fictions" (*Matter of Otis, supra*) are nevertheless two separate accounts in so far as their beneficiaries are concerned and when money ordinarily paid from income is loaned out of principal, that amount at least should be repaid to principal before any legislation can properly direct distribution to income. This seems to be the law.

*Matter of Chapal* and *Matter of Otis, supra*, fix an equitable distribution on a sale as between principal and income. Section 17-c has for its purpose a consideration of the life tenant regardless of the consequences to the principal of [fols. 149-155] the trust and without requiring that income first pay its debts to principal.

Assuming the right of the legislature to provide by statute for distribution to income beneficiaries during salvage operations, this distribution should be limited to the proportionate share of real net income after income obligations to principal have been repaid. The advances from principal for capital disbursements might be added to the principal account as an increase in capital investment and await sale for repayment but there is no justification for defeating the testamentary set-up by invasion of principal for the continuance of income.

In *Matter of Otis, supra*, the Court of Appeals, in defining an equitable doctrine, quotes with approval the opinion of Cullen, J., in *Matter of Rogers*, 22 App. Div. 428, 436. Referring to the opinion of CULLEN, J., in *Matter of Rogers*. I quote, as follows, from page 436:

"Why should each not have exactly his own so far as it is possible to ascertain it?"

This would appear to be equitable. But allocation of 3% of net income regardless of other considerations as provided by Section 17-c, subsection 2, is not giving to each what is its own.

Section 17-c, subsection 2, of Personal Property Law is unconstitutional.

Dated, New York, N. Y., January 16, 1941.

Respectively submitted Gerald P. Culkin, *Special Guardian*.

(Verified by Gerald P. Culkin, January 16, 1941.)

[fol. 156] IN SURROGATE'S COURT, COUNTY OF NEW YORK

### OBJECTIONS

Emma M. West, by her attorneys, Larkin, Rathbone & Perry, does hereby make and file the following objections to the account of City Bank Farmers Trust Company, as Trustee of the trusts created under the last will and testament of Henry C. West, deceased:

1. To the item of \$575. paid to Curtis R. Larkin on August 9, 1939, as shown by Schedule Cc, page 8, being a capital improvement, namely, for decorating, carpentry, plumbing, etc.

2. To the item of \$13.50, dated May 4, 1939, as shown by Schedule Cf, page 11, being the cost of a capital improvement, namely, a gas range.

3. To the item of \$604.07 shown by Schedule Ci-9, for reimbursement to principal of foreclosure expenses, consisting of taxes, water charges and penalties, due at the time of acquisition of the property 168 Morrison Avenue by the Trustee.

4. To the failure to allocate 3% of the net rents derived from the operation of premises 168 Morrison Avenue during the fiscal year ending March 4, 1938, namely, \$232.30, as shown by Schedule Ci-7, or of 3% of the net rents derived from the operation of said property for the period ending August 25, 1938 of \$107.87, as shown by Schedule Ci-8, to income.

[fol. 157] 5. To the failure to allot interest at the prevailing rate, for the period within which, from the time of

their receipt, said net rents were withheld from distribution to this objectant as life beneficiary.

6. To the items in Schedule Ci-9 showing the allocation as between principal and income of the cash on hand, which allots to income the inadequate sum of \$714.44.

7. To the item of \$714.44 in Schedule AII-12, under date of August 25, 1938, being the share of the proceeds of sale allocated to income, on the ground that the amount thereof is inadequate.

8. To the failure in Schedule Cj-13 to allocate to income net rents derived from the operation of property 41 Montrose Avenue, up to 3%, of the item of \$164.16 received for the period ending December 22, 1938, and the like proportionate share of the item of \$157.34 for the period ending August 9, 1939.

9. To the failure to allot interest at the prevailing rate upon said items during the period within which they were withheld from payment to this objectant as life beneficiary.

10. To the failure in Schedule AII-12 to allot to income the sum of \$118.82 received on the purchase money mortgage on 41 Montrose Avenue after resale, with interest during the period within which the items were withheld from payment.

11. To the allocation to income in Schedule Cj-14 of the inadequate amount of \$407.39, as its share in the purchase money mortgage received upon the resale of the property, [fol. 158] and to the failure to allot to income any portion of the cash received upon such resale.

12. To so much of Schedule AI-5 as fails to allot to income any portion of the amortization payments received from said purchase money mortgage on premises 41 Montrose Avenue.

13. To the items of \$407.39 allocated to income by Schedule AII-12 in said purchase money mortgage under date of August 9, 1939, and its subjection to the preference accorded to principal of a preferred interest in said purchase money mortgage in the amount of \$1,023.51.

14. To the item of net rents, aggregating \$749.73, shown by Schedule HI-1, on the ground that said rents, having



been received after the date of enactment of Section 17-c of the Personal Property Law, are payable and should be allocated to this objectant as life beneficiary up to 3% of the face amount of the mortgage in each case.

15. To the item contained in said Schedule HI of cash amounting to \$2,724.66, representing balance of income on hand, which should be paid to this objectant as life beneficiary.

Larkin, Rathbone & Perry, *Attorneys for Objectant*,  
*Emma M. West*, Office and Post Office Address,  
 No. 70 Broadway, Borough of Manhattan, City of  
 New York.

(Verified by Emma M. West, January 13, 1941).

[fols. 159-192] IN SURROGATE'S COURT, COUNTY OF NEW YORK

Before Honorable James A. Foley; Surrogate

New York, New York,

January 16, 1941.

Appearances:

Messrs. Mitchell, Taylor, Capron & Marsh, Attorneys for  
 Petitioner, City Bank Farmers Trust Company, 20 Ex-  
 change Place, New York, New York. C. Alexander Capron,  
 Esq. and James K. Taylor, Esq., Of Counsel.

Messrs. Larkin, Rathbone & Perry, Attorneys for Re-  
 spondent, Emma M. West, 70 Broadway, New York, New  
 York. Albert Stickney, Esq., Of Counsel.

Messrs. Butler, Wyckoff & Reid, Attorneys for Respond-  
 ents, Marie Elizabeth West Jones and Elizabeth Frances  
 Jones, 20 Exchange Place, New York, New York. James  
 Morrow, Esq. and also James L. Hanford, Esq., of the New  
 Jersey Bar, Of Counsel.

Gerald P. Culkin, Esq., Special Guardian for Infant Re-  
 spondents, William J. Demorest, Jr., Ann Demorest and  
 Carolyn Demorest, 31 Nassau Street, New York, New York.



## Case and Exceptions

[fol. 193]

### Will of Henry C. West

I, Henry C. West, of the City, County and State of New York, do make, publish and declare this to be my Last Will and Testament, hereby revoking any and all other wills by me at any time made.

First. I direct my just debts and funeral expenses to be paid as soon as may be after my decease.

Second. I direct that all transfer, inheritance, estate or succession taxes and death duties be paid out of my general estate as an expense of the administration thereof.

Third. I give and bequeath the sum of Two thousand five hundred dollars (\$2,500) to the Trustees for the corporation of Greenwood Cemetery of New York, and its and their successors, in trust, to invest and keep the same invested, and to apply the income therefrom to the proper care of the burial plot in said Cemetery known as the West-Emery, lot number, 2322.

Fourth. I give and bequeath to Emma M. West, my wife, the sum of Twenty-five thousand dollars (\$25,000) to be paid to her as immediately after my death as is possible.

Fifth. All the rest, residue and remainder of my estate, both real and personal, wheresoever situate, of which I may die seized or possessed, or to which I may be entitled at the time of my death, I give, devise and bequeath to The Farmers' Loan and Trust Company, a corporation organized and existing under the laws of the State of New York, in Trust, nevertheless, for the following uses and purposes: To lease said real property and collect the rents thereof, and to [fol. 194] invest and from time to time in its discretion re-invest the personal property in such securities as to it may seem proper; to collect the rents, issues and profits of all of my said residuary estate, and, after paying all necessary charges of administration, to apply the net income from said estate to the use of my wife, Emma M. West, during the term of her natural life, or until she shall remarry; provided, however, that during the life of my said wife, Emma M. West, but not after her death, there shall be first applied out of the said net income the sum of One hundred dollars (\$100) per month to the use of my brother, Zimri West. If

my said wife shall remarry, the aforesaid payment to my said brother shall continue to be made as long as my said wife lives.

Upon the death or remarriage of my said wife, my Trustee shall set aside from my residuary estate cash or securities having a then value of Thirty thousand dollars (\$30,000) and shall continue to hold and administer the same, in trust, and shall pay or apply the net income therefrom to the use of my nephew, Zimri West, 3rd, during the term of his life, and upon his death shall transfer and pay over the principal of such trust fund to my grandniece, Elizabeth Frances Jones, if she is then living, or, if she shall then be dead, shall transfer and pay over the same in equal shares per stirpes to and among her issue then living. The balance of my said residuary estate my Trustee shall continue to hold and administer, in trust, to pay or apply the net income therefrom to or for the use of my niece Marie Elizabeth West Jones, during the term of her life and upon her death shall transfer and pay over one-third of the principal of such trust fund to her daughter, my grandniece, Elizabeth Frances Jones, or, if she shall then be dead, to her issue [fol. 195] then living in equal shares per stirpes, and shall transfer and pay over the remaining two-thirds of such trust fund in equal shares per stirpes to the issue then living of my wife's niece, Wealthy Albro Lewis Demorest. If, pursuant to the foregoing provisions of this my Will, any part of my estate shall have been held in trust for a period of two lives and shall not therefore by law be eligible to be continued in trust for an additional period as directed by this Will, such part of my residuary estate shall, at the expiration of a period of two lives during which it has been held in trust, be transferred and paid over by my Trustee outright, free and discharged of any trust, to the persons otherwise entitled pursuant to the provisions of this Will to receive the income therefrom. If at any time pursuant to the provisions of this my Will any part of my property shall not have been effectually devised or bequeathed, I hereby give, devise and bequeath the same at such time to the then living issue of my wife's niece, Wealthy Albro Lewis Demorest.

Sixth, I authorize my Trustee to retain, so long as to it may seem proper, any securities left by me at the time of my decease, and also to sell the same, and, from time to time,

in its discretion, to invest and reinvest the proceeds thereof, and also any other cash at any time in its hands as Trustee, in such securities as to it may seem wise, it being my intention that in the making of new investments my said Trustee shall not be limited to the class of securities in which trustees are authorized by law to invest trust funds. My Trustee shall not be liable, or responsible for any loss resulting from the making or retention of any investment made or retained by it, in good faith.

No sinking fund shall be set aside from the income of any securities which may at any time form a part of the trust [fol. 196] funds to guard against the diminution of the premium on such securities.

Any and all stock dividends upon stocks of corporations forming part of the trust fund, payable in the stock of the corporation declaring or authorizing the same, which may be received by the Trustee at any time shall be treated and considered for all purposes as a part of the capital of the trust funds; but all extraordinary dividends or distributions other than stock dividends whether paid in bonds, cash or otherwise shall be treated as income.

Said Trustee, in its discretion, is authorized to deposit any of the securities at any time forming part of any trust estate under any plan or plans of reorganization, merger or consolidation that may commend themselves to its good judgment, and to accept the new securities which may be offered to it under any such plan or plans in exchange for such original securities, and to pay any and all assessments levied or imposed under such plan or plans of reorganization, and to charge the amount thereof against the principal of the trust estate.

I give to my Trustee full and absolute power to sell, lease, mortgage, exchange, partition or otherwise deal with any real property or interest therein of which I might die seized in like manner as I might or could do if living, and to execute all proper deeds, mortgages, leases and other instruments affecting or appertaining to said real property.

Seventh. The provisions of this Will for my wife are intended to be and shall be accepted by her in lieu of dower and all other claims in my estate.

Eighth. I nominate, constitute and appoint The Farmers' Loan and Trust Company, a corporation organized [fols. 197-201] and existing under the laws of the State of

New York, having its principal place of business at Number Twenty-two William Street, in the Borough of Manhattan; City, County and State of New York, to be the Executor of and Trustee under this my Last Will and Testament, and I direct that no bond or other security shall be required of it for the faithful performance of its duties in either capacity.

In Witness Whereof, I have hereunto set my hand and seal this 14th day of December in the year One Thousand nine hundred and twenty-eight.

Henry C. West. (Seal.)

Witnesses: Ronald Mac Lean, H. Vincent Smart, James D. Ouchterloney.

The Foregoing Instrument was signed, sealed, published and declared by the above named Testator, Henry C. West, as and for his Last Will and Testament, in the presence of us, who, in his presence, at his request and in the presence of each other, have hereunto subscribed our names as witnesses the day and year last above written, this attestation clause having first been read aloud.

Name Ronald Mac Lean. Residing at 1325 Foster Av. B'kyn, NYC.

Name H. Vincent Smart. Residing at 151 Bronxville Road, Bronxville, N. Y.

Name James D. Ouchterloney. Residing at 197-01 110th Ave., Hollis, N. Y.

[fol. 202] IN SURROGATE'S COURT, COUNTY OF NEW YORK

OPINION OF SURROGATE

(Dated March 8, 1941)

175 Misc. Rep. 1044

FOLEY, S.:

In this accounting proceeding the answers of certain of the parties and the report of the special guardian have raised numerous issues involving salvage operations of mortgaged properties acquired by a trustee by foreclosure or by deed in lieu of foreclosure. Such issues involve in part questions as to the effect of the decisions of the Court of

Appeals in *Matter of Chapal* (269 N. Y. 464) and *Matter of Otis* (276 id. 101), and in part the effect of the recently enacted Section 17-c of the Personal Property Law, which modified in certain phases the former rules in salvage operations. The briefs of the various attorneys have analyzed these questions with commendable thoroughness.

Under the terms of the testator's will, the residuary estate was devised and bequeathed in trust, "to apply the net income from said estate to the use of my wife, Emma M. West, during the term of her natural life, or until she shall remarry." Upon the death of the testator's widow, the estate was directed to be continued to be held in trust upon certain shares for the benefit of a nephew and a niece of the testator, with contingent remainders. The trust is still in effect.

At the date of his death the testator owned a number of entire guaranteed mortgages. Title to nine of the properties, upon which the mortgages were liens, was acquired by the executor either by foreclosure sale or by deed in lieu of foreclosure. By the decree of this court, dated August 10, 1936, upon an accounting by the executor, the properties so acquired were directed to be transferred by the executor to itself as trustee, as assets of the trust, to be held in separate account by the trustee. Questions as to the apportionment of the proceeds received upon the ultimate sale of the properties and the respective rights of principal and income beneficiaries in them were reserved for determination by decree in a subsequent accounting proceeding of the trustee. The trustee has now accounted for the operation of each of these properties. The account discloses that as to seven of the properties the salvage operations are still unfinished. The operation of the other two properties is complete, since they were resold prior to the enactment of Section 17-c of the Personal Property Law—one for cash and the other for part cash and part by the execution and delivery of a purchase-money mortgage. No distribution, however, has been made of the proceeds of sale of either of these properties.

The issues raised may be summarized as follows:

*First.* The constitutionality of subdivision 2 of Section 17-c of the Personal Property Law (added by Laws of 1940, Chap. 452, effective April 13, 1940) which modified, in certain respects, the prior rules in mortgage salvage operations.

*Second.* If constitutionality be sustained, the effect of the terms of that subdivision upon salvage operations falling within its scope.

*Third.* The determination of new questions not arising under Section 17-c of the Personal Property Law and not decided specifically by the Court of Appeals in *Matter of Chapal* (*supra*) and *Matter of Otis* (*supra*) or by other authorities dealing with mortgage salvage operations.

*First.* In the consideration of the constitutionality of new Section 17-c of the Personal Property Law, the prior decisions [fol. 204] of the Court of Appeals, the existing situation in trusts, the reasons and conditions which led to its enactment and the terms of the section itself become important. The *Chapal-Otis* rules had, to a great extent, simplified the problem of the trustee, the lawyer and the courts of first instance, in dealing with particular situations developed before them. But complications still remained in salvage operations.

As the economic depression subsequent to 1929 deepened and the value of real properties melted, a wave of foreclosures resulted. Mortgages, which had been regarded in former years as attractive and desirable investments for trust funds, created after foreclosure or acquisition of title complicated and difficult questions with the imposition of burdensome expense to persons interested in trust estates. The complications involved in the computation in a pending or completed salvage operation are emphasized in the pending proceeding where the mathematical analyses and the supporting schedules cover fifty-one closely typed pages of the account. The solution of these problems became the subject of study by members of the Bar and particularly by those who were specialists in the law of trusts and estates. In liaison with the Executive Committee of the Surrogates' Association of our State, intensive investigation was made with the objective of simplification of the rules applying to mortgage salvage operations. Two solutions were immediately presented. The first involved a repeal of the *Chapal-Otis* rules in their entirety, with a recommendation to the Legislature to enact a statute which would treat the foreclosed or acquired real property as a capital asset in the same manner as ordinary real estate left by a testator. [fol. 205] If the foreclosed real estate was thus treated as a capital asset, net income derived from the property would



become immediately payable to the life tenant. Upon a sale of the realty, the proceeds would be treated as part of principal. Upon such sale, no allocation between life tenant and remainderman was required. Such was the form of the statutory ~~refer~~ passed by the Legislature of Connecticut. (Pub. Acts [1939], chap. 232.)\* The obstacle to the recommendation of the passage of such a sweeping statute, despite the common sense approach which motivated it, was the belief by some of the conferees that if it were applied to mortgage investments made before the effective date of the new statute, it might be subject to the hazards of a determination of unconstitutionality. The second alternative of those who drafted and recommended the passage of the statute by the Legislature was to divide the problem into two parts. The division provided, first, for the abolition of salvage operations as to future investments in mortgages and second, with the major objective of assisting life tenants, for the modification, within constitutional limits, of the existing law as to investments in mortgages made prior to the effective date of the statutory amendment. That program was ultimately adopted and is embodied in new Section 17-c of the Personal Property Law.

Its first subdivision abolished the *Chapal-Otis* rules as to testamentary trusts of persons dying after the effective date of the statute and as to *inter vivos* trusts thereafter established. It likewise was made to apply to mortgage investments made after such effective date in existing trusts, whether testamentary or *inter vivos*. As to such trusts and mortgaged real property the new subdivision stated that [fol. 206] the "real property shall be and become a principal asset in lieu of" the mortgage. The "tenant or tenants for life or limited term shall be entitled to the net income from such acquired real property from the date of its acquisition." The rules of procedure under the *Chapal-Otis* decisions were "abolished." Any allocation or apportionment between life tenant and remainderman was prohibited. In the pending proceeding no question has arisen as to the constitutionality of such first subdivision. Indeed, no such question would be tenable since its provisions were wholly prospective in operation.

We now come to the consideration of the terms of the second subdivision of the section, the constitutionality of

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\* Supplement to General Statutes (1939), § 1291e.

which is in dispute here. Two relatively simple modifications of the *Chapal-Otis* rules were made in this subdivision. Under those rules and particularly under the language of the opinion of Judge LOUGHRAN in *Matter of Otis* (*supra*), a discretionary power was given to a trustee during a mortgage salvage operation to disburse income to the life tenant, after advances made from principal as an incident to the acquisition of the property had been repaid. It was found, however, that trustees hesitated to make any payment to the life tenant or to exercise the judicial discretion given to them by *Matter of Otis*, because of the fear of a possible surcharge in the event of an overpayment to the life tenant. The life tenant in almost every instance was the primary object of the testator's bounty. The beneficiary intended to be most favored was thus deprived, by the trustee's inaction or hesitancy, of receiving income during the entire salvage period and large sums of money were accumulated and frozen. The injustice to the life tenant was aggravated [fol. 207] by the fact that because of the lack of a ready market for the resale of the property, the salvage operation was unduly extended for a long period of years. This situation is emphasized by the facts revealed in the present proceeding. Of the seven mortgages now involved in the salvage operations in which no resale has taken place, the longest period of operation has been six years and two months. The shortest period has been four years and ten months. Thus the average period of operation of all seven mortgages has been approximately five years. In the two completed operations the periods of salvage were two years and six months and two years and eight months. This unhappy situation has been corrected by the new legislation. Trustees are expressly authorized to pay promptly net income derived from the foreclosed or acquired property up to three per centum per annum upon the face amount of the mortgage. From the time of the passage of the new act, it has been the practical experience and observation of the Surrogates that hundreds of thousands of dollars which had been theretofore accumulated, were paid out to life tenants upon the authority granted by the statute. Where the trustee had paid the yearly income up to the three per cent maximum to the life tenant, the statute made the payment final. It was specifically stated by the Legislature that such payment up to the maximum was "not subject to

recoupment from the life tenant or as a surcharge against the trustee or executor." Moreover, under the new statutory rule, net income up to the maximum of three per cent became payable from the very beginning of the salvage operation, that is, from the date of acquisition by foreclosure or by deed in lieu of foreclosure.

[fol. 208] The other amendment to the *Chapal-Otis* rules made by the second subdivision of the new section in the balancing of the equities, furnished protection to the remaindermen interested in the principal of the trust. Excess net income earned in any one year during the salvage operation above the three per cent maximum payable to the life tenant, was directed to be applied to advancements from principal for arrears of taxes and other liens which accrued prior to the foreclosure or acquisition in lieu of foreclosure and to the cost of capital improvements. Where any balance of unpaid principal advances remained due at the close of the salvage operation, such balance was declared to be "a primary lien upon the proceeds of sale and shall be paid first out of any cash so derived. If insufficient the balance shall be a primary lien upon any purchase money mortgage received upon the sale."

The special guardian of the infant remaindermen has, perhaps, by way of formal objection with a view to a review of this decision by the appellate courts, raised the issue of unconstitutionality. By that procedure it is hoped by all those interested in this program of law reform, that the constitutionality of the new statute will be forever quieted. In essence, therefore, this proceeding is to be regarded as a test case. The special guardian contends that the new statute deprives his wards of property rights and that it is violative of the due process clause of the Fourteenth Amendment of the Federal Constitution and of the similar clause contained in our State Constitution.

His specific attack is based upon the retroactive provisions of the new second subdivision which apply to mortgage investments made previous to its enactment or to salvage operations initiated prior to such enactment. It provides: "The terms and rules of procedure of this subdivision shall apply specifically (a) to the estate of persons dying before its enactment and (b) to mortgages on real property held by a trustee under a deed of trust or other instrument executed before the date of its enactment and (c) to real property acquired by foreclosure of mort-

gage or real property acquired in lieu of foreclosure before or after the date of its enactment in trusts created or mortgage investments made prior thereto, and (d) to any pending proceeding or action for an accounting of the transactions of an executor or trustee." It is claimed that the effect of that subdivision was to take away property from the remainderman in so far as the amounts paid to the life tenant up to the maximum of three per cent per annum might exceed the income allocable to him under the *Chapal-Otis* rules at the close of the mortgage salvage operations.

All of these contentions are overruled. The provisions of the new subdivision are merely remedial, procedural and administrative. The Legislature has done no more in formulating a modification of existing rules than the courts themselves could do and have done within their constitutional powers. In a general sense the rules as to these salvage operations have been in a fluid state and have never been absolutely or finally fixed by the courts in their application to existing trusts or prior salvage operations. The strongest support for that conclusion is found in the opinion of Judge Loughran in *Matter of Otis* (*supra*). He there stated, "Perhaps it should be added that a general rule for such situations cannot be attained at a bound, that no rule [fol. 210] can be final for all cases and that any rule must in the end be shaped by considerations of business policy. Accordingly, we have here put aside inadequate legal analogies in the endeavor to express fair, convenient, practical guides that will be largely automatic in their application. Only the sure result of time will tell how far we have succeeded." (*Matter of Otis, supra*, p. 115.) The "sure result of time" had led the Legislature to make the changes of procedure upon the ground of necessity and advisability by the enactment of the new subdivision. The traditional tests of a statute are the old law, the mischief and the remedy. It is the duty of the courts so to construe the act as to suppress the mischief and advance the remedy. The legislative purpose was declared in the statute itself in subparagraph (d) of subdivision 2 of the section. It reads: "The purpose of the enactment of this subdivision is declared to be the simplification of the rules of procedure in mortgage salvage operations and the elimination of present complications which work to the disadvantage of the life tenant, who is usually the principal object of the testator's

or settlor's bounty, by depriving him of a fixed right to the actual payment of any net income earned by the property. Such fixed right is granted in lieu of the discretion now given to the trustee to pay net income or any part thereof to the life tenant. The general rules of the apportionment of the proceeds of sales between life tenant and remainderman are retained subject to the express modifications made herein. Only equitable adjustments and balances as between the parties are intended to be effectuated by the provisions of this subdivision."

[fol. 211] The additional reasons which moved the Legislature to modify the existing rules under the *Chapal-Otis* decisions are stated in the explanatory note which was printed in the legislative bill. It is indicative of the intent of the Legislature. It reads in part: "The *Chapal-Otis* rule authorizes the trustee to pay surplus net income in his discretion. Trustees have hesitated to pay such net income because in the case of overpayment to the life tenant, the trustee might be surcharged with that amount. The life tenant of the trust must wait in the majority of cases for a long period of time before he becomes entitled to the payment of any income, because of the present requirement that advances from principal for the expenses of foreclosure and for arrears of taxes and other liens must first be paid from the net income of the property. The amendment provides for the immediate payment of income to the life tenant beginning with the date of the acquisition of the property by the trustee by foreclosure or conveyance in lieu of foreclosure."

Again, the nature of a salvage operation was described in *Matter of Otis* (*supra*); as a resort to fictions. "Both capital account and income account, as described in the *Chapal* case, are fictions. \* \* \* If, then, the remaindermen are to participate in the apportionment on the feigned basis of unimpaired principal, the share of the life tenant should be computed on the same assumption. The invention of the 'original investment' is no more valid than the invention of 'unpaid interest' thereon. Indulgence in both fictions keeps the balance even between the respective parties in interest." Under the "historic fictions" of the Eng- [fol. 212] lish law and the modern fictions which exist under our own law, their ineptness have led to change and improvement by the courts which had to apply them. This



very ineptness also constituted an invitation to Parliament in England, and to our own Congress and Legislatures, to alter the fictions, particularly in procedural matters, in order to correct injustice. Fictions, as stated by Professor Gray, were invented and altered "in order that the wine of new law might be put into the bottles of old procedure." (Gray, *The Nature and Sources of the Law*, p. 34.) The fiction was always capable of modification to meet the needs of modern justice.

Alterations of rules of procedure or administration made by the Legislature or by the courts, do not change substantive rights. Rules of procedure may, therefore, be modified, added to or repealed as the exigencies of the law and particular situations require. "Nor has a person a vested interest in any rule of law entitling him to have the rule remain unaltered." (*Preston Co. v. Funkhouser*, 261 N. Y. 140; *affd.*, *sub nom. Funkhouser v. J. B. Preston Co.*, 290 U. S. 163, citing *Truax v. Corrigan*, 257 id. 312, 348.)

It is claimed that the effect of subdivision 2 of Section 17-c was to take away property from the remainderman, in so far as the amount ultimately payable to him on a sale of the real property might be less than the amount which would be payable to him under the rules laid down in *Matters of Chapal* (*supra*) and *Matter of Otis* (*supra*). The possibility that such a situation might result is infinitesimal. Two factors show the extreme improbability of the occurrence of such an event. The customary mortgage interest rate for several years past has been five per cent per annum. [fol. 213] The maximum amount payable to the life tenant, under the new statute, is three per cent. There is, therefore, a margin of safety of two per cent available in the average case in the final computation of allocation to income. Again, a property which would yield three per cent net per annum would, in all probability, produce a selling price sufficient to pay the life tenant, after final apportionment, a sum in excess of what had been paid within the statutory maximum during the period of the salvage operation.

Many remedial rules of procedure or administration have created new rights not theretofore existing, which ultimately benefited one person as against another. The constitutionality of such legislation, even though it were retroactive in its application to existing actions or proceedings



or to the estates of those dying before the statutory change was enacted, has been time and again sustained by the courts in the interest of uniformity and justice. As, for example, in *Preston Co. v. Funkhouser* (*supra*), our Court of Appeals and the United States Supreme Court upheld, as constitutional, a statute retroactive in scope providing that in any action for the enforcement of or based upon breach of performance of a contract, interest shall be allowed upon the sum awarded, whether theretofore liquidated or unliquidated. In that case the Court of Appeals, through Judge Pound, said: "Every change in the remedies open to parties to a contract does not constitute an impairment of its obligation. Where the statute deals only with the remedy, the creation of a new and more adequate remedy does not impair the obligation of the contract. (*Sackheim v. Piqueron*, 245 N. Y. 62.) \* \* \* It follows that Section 480 is a [fol. 214] remedial statute to be construed, according to its literal meaning to apply to all actions brought after it went into effect irrespective of the time when the cause of action arose. It changes an existing right of action rather than creates a new right." The court also pointed out that "the mere fact that the statute is retroactive does not bring it in conflict with the Federal Constitution."

It has always been the recognized function of the courts to promulgate rules of procedure and administration for the guidance of fiduciaries in their conduct of trust estates. Such rules have also found expression from time to time by enactment in the various statutes of our State. Examples of remedial statutes modifying or establishing rules of procedure in the administration of existing trusts, where their reasonableness and constitutionality have been sustained, are many. In *Matter of Robertson v. de Brulatou* (188 N. Y. 301), after the death of the testator, the Legislature established a new and different rule covering the compensation of trustees. An increased measure of compensation was provided. The trustees were held to be entitled to their benefit and commissions were allowed to them under the statute in effect at the date of the accounting. In *Matter of Barker* (230 N. Y. 364), commissions for receiving assets were allowed to the estates of deceased executors pursuant to a statute in effect at the date of the accounting but which was not enacted until subsequent to the death of the executors, and necessarily of the testator. In re-

ferring to the retroactive effect of the statute, the court there said: "The general rule is that the fees of an executor are to be fixed by the rules and law which prevail at the time when they are settled. (*Robertson v. de Brulatour*, [fol. 215] 188 N. Y. 301, 316, 317; *Whitehead v. Draper*, 132 App. Div. 799.) In the last case this principle was applied in the opinion written by Justice McLaughlin in a case where the statute invoked in aid of an executor's commissions was not passed until after his death. This is quite akin to the rule that remedies will be applied in accordance with the law which prevails at the time when relief is sought rather than at the time when the injury arose. (*Matter of Berkowitz v. Arbib & Houlberg, Inc.*, 230 N. Y. 261.)"

Other instances of remedial statutes may be found in (1) those modifying, after the death of the decedent, the classes of legal securities in which trustees are authorized to invest (*City Bank Farmers Trust Co. v. Evans*, 255 App. Div. 135; *Matter of Hamersley*, 152 Misc. 903); (2) the provisions of the Surrogate's Court Act (§§ 225 and 226), providing that an administrator with the will annexed or a successor trustee may exercise powers granted to an executor or trustee to mortgage, lease or sell real property (*Hollenbach v. Born*, 238 N. Y. 34); (3) the sections of the Real Property Law authorizing the sale of real property where the interests are both possessory and future (*Matter of Mercereau*, 233 N. Y. 540; *Matter of Gaffers*, 254 App. Div. 448) and (4) the statute granting a creditor of an income beneficiary of a trust the right to require that ten per cent of the income be applied in satisfaction of his claim of debt. (*Brearley School v. Ward*, 201 N. Y. 358.) The constitutionality of each of these legislative enactments was sustained.

In *Reiner v. Fidelity Union Trust Co.* (126 N. J. Eq. 78, [fol. 216] 8 A. [2d] 175; rev'd. on other grounds, 127 N. J. Eq. 377, 13 A. [2d] 291) a statute giving the Court of Chancery of the State of New Jersey power to authorize or direct trustees to invest in securities other than those listed by the statutes as legal for trust investments was upheld as constitutional. The court there said: "The statute does not purport to authorize the court to change substantive rights. It has reference merely to matters of administration."

The extent to which courts have gone to sustain rules of procedure and administration is evidenced by the decision of the United States Supreme Court in *Kuehner v. Irving Trust Co.* (299 U. S. 445): There, the constitutionality of clause (10) of subsection (b) of section 77B of the Bankruptcy Act (U. S. Code, tit. 11, § 207), which limited the claim of a landlord for indemnity under a covenant in a lease in a corporate reorganization to an amount not to exceed three years' rent, was considered. Prior to the passage of this provision of the Bankruptcy Act, such claim was not provable or dischargeable in a bankruptcy proceeding. Under the new statute, the landlord's claim was allowed to the extent of three years' rent only. The rental value for the balance of the term of the lease under the rent fixed by the lease greatly exceeded the three years' rent allowed. It was asserted that this limitation offended the due process clause of the Fifth Amendment of the Constitution of the United States. The validity and constitutionality of the statute were sustained as giving a new and more certain remedy for a limited amount in lieu of an old remedy, insufficient and uncertain in its result. The statute was held to be fair and reasonable and to create uniformity of treatment of a peculiar class of claims, difficult of liquidation. It was held not to be the taking of the landlord's property without due process of law.

As applied to existing trusts, the above authorities clearly support the validity of the remedial legislation enacted in subdivision 2 of Section 17-c of the Personal Property Law.

The rules under the subdivision are just, fair and reasonable. Only equitable adjustments and balances as between principal and income beneficiaries were declared to be effectuated by its provisions. It was within the province and power of the Legislature to enact them. The objection of the special guardian, therefore, addressed to the constitutionality of the statute is overruled.

*Second.* Such determination of constitutionality requires the surrogate to pass upon the various questions raised as to the effect of the terms of the new subdivision upon mortgage salvage operations within its scope. These questions are stated and discussed *seriatim* as follows:

(a) Does the section apply to the salvage operation of property acquired by a trustee which was sold before April

13, 1940, the effective date of the statute, where the distribution has not been closed by a decree upon a judicial settlement of the account or by a written or other valid agreement between the parties for a voluntary distribution?

The Surrogate holds that where the salvage operation has been completed before the effective date of the new section, its terms do not in any way alter or change the rights of the parties. Once the salvage operation is finished before that date, there remains nothing to be done except to make the computation of apportionment and to distribute under the *Chapal-Otis* rules. The terms of the statute apply only to uncompleted salvage operations at the date [fol. 218] of its enactment or to operations initiated subsequent to such date.

(b) As to operations uncompleted at the effective date of the new section, shall payments to the life beneficiary of net income, when earned, up to a maximum of three per cent per annum upon the face amount of the mortgage be computed upon an annual basis, or shall the entire period of operation, if extending over a period of more than one year, be considered in such computation?

The answer is obvious. The statute clearly contemplates that the net income payments shall be based upon the annual income of the property and not upon the income for the entire period of the unfinished operation. It provides (Pers. Prop. Law, § 17-c, subd. 2, par. [a]): "Net income during the salvage operation up to three per centum *per annum* upon the principal amount of the mortgage shall be paid to the life tenant \* \* \*." (Italics mine.) Annual rests and annual balancings of the account must thus be employed and the result of the operation of each parcel of property for each year must be treated as a separate entity in the computation and payment of the maximum net income permitted by the statute to be paid to the life beneficiary. It is an elementary rule in the administration of trusts that the computation of net income payable to a life tenant is based upon the yearly period, unless the terms of the will fix some other period. Any other policy would permit serious prejudice on the part of the trustee as against the life tenant by the withholding of accumulated income.

If, therefore, under this method of computation there are deficits of net income in lean years, they may not be made up from surplus net income in productive years. Income earned in any one year in excess of the three per cent [fol. 219] maximum payable to the life beneficiary and after repayment of principal advances, must be retained. Under the new section, principal advances "shall be repaid out of excess net income above such three per centum per annum. When principal advances have been satisfied, any excess income shall be impounded \* \* \* to await sale and apportionment." If the payments of income to the life beneficiary were not based upon annual rests, and the deficiency of net income payments in lean years could be satisfied from excess income in good years, the provision of the statute that such excess income shall be impounded would be nullified.

(c) In the computation of the net income payable to the life beneficiary, shall the fiscal year beginning with the date of the acquisition of the real property be used or shall the calendar year be employed?

I hold that the anniversary date of the computations of the annual payments to the life beneficiary is the date of the acquisition of the real property and the annual rests shall be based upon that date. The period of salvage begins from the date of acquisition of the mortgaged property. (*Matter of Otis, supra.*) The net income payable to the life beneficiary must be computed upon rents received during the fiscal year beginning with that date. It is not based upon rents received during the calendar year. The explanatory note printed in the legislative bill states: "The amendment provides for the immediate payment of income to the life tenant beginning with the date of the acquisition of the property by the trustee by foreclosure or conveyance in lieu of foreclosure." The statute provides that net income shall be paid during the salvage operation. The annual accounts and the computation of the amount [fol. 220] due the life tenant at the statutory rate up to three per centum per annum must be based upon the recurring periods of one year from the anniversary dates of acquisition.

(d) Where net rents up to a maximum of three per cent per annum have been paid to a life beneficiary during the period of salvage, has the new section changed the method



of apportionment to be made after sale, as laid down by the rules in *Matter of Chapal* (*supra*) and *Matter of Otis* (*supra*)? In other words, has the formula for the allocation, as between income and principal, been changed by the terms of the new section? The Surrogate holds that no change was intended by the Legislature.

The new section merely makes mandatory the payments of three per cent of net income each year to a life beneficiary when earned. It does not, however, change the formula for ultimate apportionment of the net proceeds of the salvage operation between life beneficiary and remainderman. Again the new subdivision provides: "The existing rules of procedure applying to salvage operations respecting existing mortgage investments are continued except as modified by the subparagraphs hereinafter set forth." As stated in *Matter of Chapal* (*supra*): "In such an investment situation what is involved is the salvage of a security. The security \* \* \* is a security not for principal alone but for income as well." Paragraph (a) of subdivision 2, with a view to protecting the interests of both life tenant and remainderman in such securities and to impartial and fair apportionment, provides as follows: "The amount of all such payments shall be taken into account, however, in the apportionment of the proceeds of sale and shall be charged against the share of the life tenant." All net income, [fol. 221] come, therefore, including such as had been paid to the life beneficiary during the salvage period, must be added to the proceeds of sale of the property as the total salvage fund. Out of such total there shall first be deducted the amount required for repayment of principal advancements. The balance then remaining shall be apportioned according to the *Chapal-Otis* formula between income and principal. After the share due the life beneficiary has been computed upon such apportionment, there shall first be credited upon such share the net amounts of rents paid to the life beneficiary during the salvage operation as an advancement to income. The amount so paid to the life beneficiary must be "charged against the share of the life tenant" under the new section. The amount apportioned to income, less the income advanced to the life tenant, shall be the balance to which the life tenant shall then be paid out of the proceeds of the salvage operation. This method of determining the ultimate shares allocable to income and principal unquestionably, in my opinion, accords with



proper accounting practice. (*Matter of Chapal, supra; Matter of Otis, supra; Matter of Brainerd*, [WINGATE, S.] 169 Misc. 640, 644.)

*Third.* The questions presented for determination in this group do not arise out of the provisions of the new section. They involve problems that have not directly been passed upon by the *Chapal-Otis cases* or by other authorities.

(a) Where a trustee has taken over property under foreclosure or by deed in lieu of foreclosure and finds it in such condition as to require rehabilitation, are the expenses incurred to put the property in a tenantable condition exclusively capital charges to be treated as advancements from [fol. 222] principal, or are they income charges?

The Surrogate holds that where at the time of the acquisition of the real property, the premises were not in rentable condition the cost of putting them into such condition is payable out of principal. The cost of thereafter maintaining the premises in repair and in tenantable condition is payable out of income. Under the new paragraph (a) of subdivision 2, the "cost of all capital improvements" is made a principal charge.

As applied to ordinary trust property where no salvage operation is in effect, the rule seems generally to be well settled that where real property is originally received by the trustee in an untenable condition, the cost of rehabilitation is chargeable against principal. (*Restatement of the Law of Trusts*, comment i, § 223; *Sterens v. Melcher*, 152 N. Y. 551; *Matter of Deckelmann*, 84 Hun, 476; *Matter of Snyder*, 138 Misc. 873; *Smith v. Keteltas*, 62 App. Div. 174; *Matter of Heroy*, 102 Misc. 305.)

In the *Restatement of the Law of Trusts* the following appears: "The cost of putting into tenantable repair premises which were not in such repair when received by the trustee, whether originally acquired by the trustee as part of the trust property at the time of the creation of the trust or subsequently acquired by him, is payable out of principal; but the cost of thereafter keeping the premises in repair is payable out of income." The application of this rule to salvage operations would appear to be for the best interests of both life beneficiary and remainderman. Whenever necessary repairs or structural changes are made to put real property in a rentable condition, there inures a

benefit to both principal and income beneficiaries. The ex-[fol. 223] penses of rehabilitation, therefore, which are incurred upon the acquisition of the property should be treated as advancements from principal and charged to principal. On the other hand, all expenditures for current repairs and those which are incidental to the management of the property, during the period of the salvage operation, should be charged to income under the general rule laid down in *Matter of Albertson* (112 N. Y. 434). The Surrogate sustains the objections of the special guardian to the payment from principal of sums for the current repair and maintenance of the premises, other than the expenses of putting them into tenable condition at the date of the acquisition of the property. If the parties are able to agree as to the items properly chargeable to income under this determination, a stipulation may be filed within ten days of this decision. If agreement is not reached, the matter will be set down for a further hearing upon this issue.

(b) The further question has been raised as to what is the method of apportioning dividends which may be received in payment, partially or in full, of claims arising out of the guaranty against loss resulting from a defaulted mortgage by an insolvent mortgage guaranty company. Certain sums have been received by the trustee in this estate on claims allowed by the Superintendent of Insurance, as liquidator of the Bond and Mortgage Guarantee Company. All of the properties involved were acquired by foreclosure or by deed in lieu of foreclosure prior to December 31, 1937. The order of liquidation was made and the rights of the parties under the Insurance Law are to be determined as of that date.

[fol. 224] The obligation of the Bond and Mortgage Guarantee Company constituted a guaranty as to both interest and principal. The trustee filed proofs of claim with the Superintendent of Insurance. These claims covered the deficit of interest up to December 31, 1937, and the alleged liabilities of the guarantor for restitution of principal losses. In each case the default in interest was allowed by the Superintendent in full. The claims for principal charges were substantially reduced by him.

The Surrogate holds that liquidating dividends when received must be treated as part of the general funds developed from the salvage operation. In this sense they are

like rents received and the proceeds of sale of the acquired real property. The allocation made by the Superintendent of Insurance as between the guaranty of losses incurred in income and the guaranty of losses incurred in principal is to be treated as tentative only. In addition, all of the parties here conceded that because of the very large liabilities of the guaranty company, the dividends will be relatively small in amount. Moreover, the application of these liquidating dividends should be made as simple as possible.

With this objective in mind the Surrogate holds that as to dividends received for income losses from the Superintendent of Insurance, such amounts should be added to the income (derived as rents) during the specific year of the actual reception of the liquidating dividends. This addition to such rents may still leave a deficit in operation with no *net* rents available for the fiscal year. On the other hand, the addition may wipe out a deficit and produce a net income for such year. In the latter case the moneys become payable within the three per cent maximum to the life [fol. 225] tenant. If there be any surplus above the three per cent maximum caused by the addition of these dividends, such surplus shall, under the rule of Section 17-c, be applied on account of advances to principal, or if such advances have been satisfied, they shall be retained as part of the general funds of the salvage operation to await sale and final apportionment.

Any dividends received from the Superintendent of Insurance as tentative payments upon principal account shall likewise be retained as part of the general proceeds of the salvage operation to await final sale and apportionment, unless necessary to discharge unpaid balance of principal advancements.

Any dividends which may be received by the trustee on its claim under the guaranty of a mortgage subsequent to the completed salvage of such mortgage, should likewise be apportioned between principal and income in the same ratio as has been applied to the proceeds of sale. They are additional proceeds of the salvage operation.

(c) Where the mortgage was originally guaranteed as to payment of interest and principal by a mortgage guaranty corporation and the guaranty has been canceled by the trustee, because of the insolvency of the corporation,

shall the share of the life beneficiary be computed upon the rate fixed in the mortgage or at the rate agreed to be paid by the guaranteeing corporation? In other words, assume an original mortgage was made with six per cent interest. The corporation has reserved to itself, as the usual charge for the guaranty, one-half of one per cent per annum. The purchaser of the mortgage from the corporation [fol. 226] became originally entitled to five and one-half per cent. Where the agency of the guarantor has been canceled, is the share of the life beneficiary to be computed for the duration of the period of salvage at six per cent per annum, the rate set forth in the instrument or at five and one-half per cent?

I hold that the rate of interest fixed in the mortgage taken over by the trustee from the guaranty company is the rate upon which the life beneficiary's interest must be computed. The Court of Appeals in *Matter of Otis* (*supra*) declared the rate of interest as fixed in the mortgage to be the rate to be used as a basis upon which allocation to income was to be made. It said: "We prefer to adhere to our ruling in *Meldon v. Berlin* (167 N. Y. 573, affg. 31 App. Div. 146) that interest should be computed at the mortgage rate for the whole period." Although the Court of Appeals in that case did not have before it the exact question here involved, its preference to the adoption of a rule which would fix the mortgage rate upon the cancellation of a guaranty, would appear to be clearly indicated. In view of the determination in *Matter of Otis* (*supra*), it is immaterial that only a yield of five and one-half per cent was guaranteed by the guaranty corporation.

Where, however, prior to acquisition by foreclosure or by deed in lieu of foreclosure, the trustee and the owner of the property have by agreement fixed a rate of interest below the rate prescribed in the mortgage instrument itself, the reduced rate shall be used and not the mortgage rate. Such agreement for reduction of interest, if validly made, is binding upon the parties.

In the present proceeding, the trustee, by letter dated [fol. 227] October 22, 1934, agreed to reduce the interest rate in the mortgage on one parcel of real property, 240 Floyd street, Brooklyn, N. Y., from six per cent to four per cent. The interest of the life tenant in the salvage operation must, therefore, be computed at the latter rate from the date of such reduction to the date of sale.

(d) Further questions have been presented as follows:

Where there has been a resale of the foreclosed property and a purchase-money mortgage has been taken back, shall amortization payments under the new mortgage received by the trustee be applied primarily to the discharge of unpaid principal advances for the prior salvage operation, if any are still due? Where principal advances have been entirely repaid, shall amortization payments on the purchase-money mortgage be allocated between life tenant and remainderman as fixed upon apportionment of the proceeds of sale, pursuant to the applicable rules, upon the completion of the prior salvage operation?

The answer to each of these two questions must be in the affirmative. Since unpaid principal advances are a prior lien upon the proceeds of sale of the salvaged property (*Matter of Chapal, supra*; *Matter of Otis, supra*; Pers. Prop. Law, § 17-c), principal has a prior interest in or lien upon the purchase-money mortgage taken back by the trustee upon the sale. In those circumstances, amortization payments made by the new mortgagor should be credited entirely to principal on account of such prior lien. When the principal advances have been entirely repaid, the amounts received for amortization should be apportioned between principal and income in accordance with the respective shares of each, previously computed and apportioned under the *Chapal-Otis* rule. The interest received [fols. 228-234] by the trustee on the purchase-money mortgage I hold is payable to the life beneficiary. A similar conclusion was reached in *Matter of Martin* (165 Misc. 597).

(e) One further question requires disposition. It is claimed by the income beneficiary that she should be allowed interest at the prevailing rate upon the rents withheld from her by the trustee, which were distributable under section 17-c, from the date of their receipt by the trustee until their payment. The claim is disallowed. The Surrogate holds she is entitled to no interest on such rents under the circumstances of this proceeding. In a case where the trustee arbitrarily refuses to pay, interest might be awarded against him for his recalcitrancy and by way of compensation for the detriment suffered by the life tenant.



The objections filed to the account herein are disposed of as follows:

Objections I, II, III, IV, V and VII filed by the special guardian are overruled. Objection VI, relating to the charging of expenditures for repairs, has been the subject of instructions and possible further hearing in the prior portion of this decision.

Objections 5 and 9 of the life beneficiary are overruled. The remaining objections filed by her are sustained to the extent of directing the necessary readjustments to be made in the account to comply with the conclusions of the Surrogate contained in this decision.

Submit decree on notice settling the account in accordance with this decision and with the prior decision construing the will (175 Misc. 1042) made in this proceeding.

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[fol. 235] IN SURROGATE'S COURT, NEW YORK COUNTY

NOTICE OF APPEAL TO COURT OF APPEALS OF INFANT APPELLANTS, WILLIAM J. DEMOREST, JR., ANN DEMOREST AND CAROLYN DEMOREST

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Please take notice that the infants William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, and the undersigned, as special guardian of the said infants, hereby appeal to the Court of Appeals from the resettled order herein of the Appellate Division of the Supreme Court for the First Department, dated and entered in the Office of the Clerk of said Appellate Division on April 16th, 1942, unanimously affirming the final decree herein of the Surrogate's Court, of the County of New York, made and entered [fols. 236-244] on September 9th, 1941, and that said infants and the undersigned as special guardian, hereby appeal from said order of the said Appellate Division insofar as it sustains the constitutionality of Section 17-e, subdivision 2, of the Personal Property Law of the State of New York.

Dated: New York, N. Y., April 16th, 1942.

Gerald P. Culkin, *Special Guardian*.

To: Larkin, Rathbone & Perry, Esqs., *Attorneys for Emma M. West, Appellant-Respondent*, Office and P. O. Address,



70 Broadway, New York City. Mitchell, Taylor, Capron & Marsh, Esqs., *Attorneys for City Bank Farmers Trust Company, as trustee, etc., Respondent* 20 Exchange Place, New York City. Butler, Wyckoff & Reid, Esqs., *Attorneys for Marie Elizabeth West Jones and Elizabeth Frances Jones, Respondents*, 165 Broadway, New York City.

[fol. 245] IN SUPREME COURT OF NEW YORK, APPELLATE  
DIVISION

Present: Hon. Francis Martin, *Presiding Justice* Hon. Alfred H. Townley, Hon. Edward J. Glennon, Hon. Edward S. Dore, Hon. Joseph M. Callahan, *Justices*.

In the matter of the Judicial Settlement of the Account of Proceedings of City Bank Farmers Trust Company as Trustee of the trusts created under the Last Will and Testament of Henry C. West, Deceased, and of the Application of City Bank Farmers Trust Company as Trustee as aforesaid, for a Determination as to the Construction and Effect of said testator's Last Will and Testament, and for Instructions and Directions as to the Manner and Method of Allocation and Distribution of the Funds which are now or may hereafter be in its hands as Trustee as aforesaid.

William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, *Infant Appellants*, Emma M. West, *Appellant*, City Bank Farmers Trust Company, as trustee, etc., *Respondent*, Marie Elizabeth West Jones and Elizabeth Frances Jones, *Respondents*.

ORDER AS RESETTLED—Dated April 16, 1942

[fol. 246] A motion having been made by Gerald P. Culin, special guardian for William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, infant appellants herein, for a resettlement of the order made herein and entered and filed in the office of the Clerk of this Court on the 2nd day of April, 1942, and Emma M. West, City Bank Farmers Trust Company, as trustee under the last will and testament of Henry C. West, deceased, Marie Elizabeth West Jones and Elizabeth Frances Jones having waived notice of said

motion and approved of such resettlement of said order;

Now, upon reading and filing the annexed affidavit of Gerald P. Culkin, sworn to the 8th day of April, 1942, and the annexed waiver of notice and approval of such resettlement, it is

Ordered that said order be and the same hereby is resettled to read as follows:

[fol. 247] At a term of the Appellate Division of the Supreme Court held in and for the First Judicial Department in the County of New York, on the 2nd day of April, 1942.

Present: Hon. Francis Martin, *Presiding Justice*, Hon. Alfred H. Townley, Hon. Edward J. Glennon, Hon. Edward S. Dore, Hon. Joseph M. Callahan, *Justices*.

[fols. 248-249] An appeal having been taken to this Court by Gerald P. Culkin, as Special Guardian for the infant appellants William J. Demorest, Ann Demorest and Carolyn Demorest, from a decree of the Surrogate's Court of the County of New York entered in the Surrogate's Court on the (9th) day of September, 1941, except so much thereof as determines the true meaning and construction of the Fifth Clause of the last will and testament of Henry C. West, deceased, and directs the disposition of the income from the trust created under said clause, to wit, paragraph "1" to "4" thereof, and excepting so much of said decree as fixes the amount and directs the payment of costs, disbursements, fees, and allowances to counsel and Special Guardian;

And an appeal having been taken by Emma M. West from so much of said decree as is specified in her notice of appeal,

And said appeal having been argued by Mr. Francis J. Mahoney of counsel for Gerald P. Culkin, Special Guardian for the infant appellants, by Mr. Albert Stickney of counsel for Emma M. West appellant and respondent, and by Mr. C. Alexander Capron of counsel for the respondent trustee; and due deliberation having been had thereon;

It is hereby unanimously ordered and adjudged that the decree so far as appealed from be and the same is hereby affirmed, with costs to the respondent trustee and one bill of costs to the infant appellants, William J. Demorest, Jr., Ann Demorest and Charles Demorest, payable out of the fund.

Enter, A. H. T.

[fol. 250] STIPULATION WAIVING CERTIFICATION OF RECORD  
TO COURT OF APPEALS

Pursuant to Section 170 of the Civil Practice Act, it is hereby stipulated that the foregoing consists of true copies of the notice of appeal to the Court of Appeals of William J. Demorest, Jr., Ann Demorest and Caroline Demorest, infants, and their special guardian Gerald P. Culkin, Esq.; the notice of appeal to the Court of Appeals of Emma M. West; the order of the Appellate Division granting leave to appeal to Emma M. West; the order of the Appellate Division affirming the decree of the Surrogate's Court dated April 2, 1942; the order of the Appellate Division dated April 16, 1942, resettling said order dated April 2, 1942, and all of the papers on which the courts below acted on making said order of affirmance, all of which are now on file in the office of the Clerk of the Surrogate's Court, County of New York, or the office of the Clerk of the Appellate Division of the Supreme Court, First Department. Certification thereof is hereby waived.

Dated: May 14, 1942.

Gerald P. Culkin, Special Guardian for Infant Appellants; Larkin, Rathbone & Perry, Attorneys for Emma M. West, Appellant; Mitchell, Taylor, Capron & Marsh, Attorneys for City Bank Farmers Trust Company, as Trustee, etc., Respondent; Butler, Wyckoff & Reid, Attorneys for Marie Elizabeth West Jones and Elizabeth Frances Jones, Respondents.

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[fol. 251] Certificates to opinion of Court of Appeals omitted in printing.

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[fol. 252] IN COURT OF APPEALS OF NEW YORK

In the Matter of the Estate of Henry C. West, Deceased:  
WILLIAM J. DEMOREST, JR., et al., Appellants; CITY BANK  
FARMERS TRUST COMPANY, as Trustee, et al., Respondents

Appeal by William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, infants, and their special guardian,

from an order of the Appellate Division of the Supreme Court in the first judicial department, entered April 16, 1942, which unanimously affirmed, so far as appealed from, a decree of the New York County Surrogate's Court (Foley, J.) settling the accounts of City Bank Farmers Trust Company, as trustee under the will of Henry C. West, deceased, and construing the will of the testator. The appeal is from such order of the Appellate Division in so far as it sustains the constitutionality of subdivision 2 of section 17-c of the Personal Property Law (Cons. Laws, ch. 41).

Appeal by Emma M. West, by permission, from so much of such order of the Appellate Division as unanimously affirmed portions of the decree contained in articles 6, 7, 21, 22 and 26 thereof.

*Francis J. Mahoney* for Gerald P. Culkin, as special guardian for William J. Demorest, Jr., et al., infants, appellants.

*Albert Stickney* and *Albert J. Maginnis* for Emma M. West, appellant and respondent.

*C. Alexander Capron* and *J. Karr Taylor* for City Bank Farmers Trust Company, as trustee, respondent.

#### OPINION—January 14, 1943

FINCH, J.:

The question presented for decision is the constitutionality and construction of the provisions of subdivision 2 of section 17-c of the Personal Property Law (L. 1940, ch. 452, effective April 13, 1940; Cons. Laws, ch. 41) in so far as the same modify retroactively the rules relating to mortgage salvage operations.

The new statutory rules allot to the life tenant out of the net income earned from the operation of real estate in salvage, an annual amount up to three per cent of the face value of the mortgage investment. Such right is granted in lieu of the discretion vested in the trustee under the heretofore existing rules of trust administration to pay net income or any portion thereof to the life tenant, a discretion which has not been exercised generally by trustees through fear of possible surcharge. Such payment of net income is made payable from the beginning of the salvage operation and is declared to be final and not subject to recoupment, either from the life tenant, or from the trustee or executor by way of surcharge. With the exception of the aforesaid modification, the previously existing rules governing sal-

vage operations are continued except that annual net income in excess of the maximum sum payable to the life beneficiary, is directed to be held and further equitable adjustments upon the apportionment are also provided for, in order to insure to the remainderman that any unpaid advances from principal must be first repaid upon the final liquidation of the investment.

[fol. 253] The validity of this statute has been put in issue upon this proceeding for an intermediate accounting by the trustee under the will of Henry C. West. By the terms of the testator's will, his residuary estate was devised to a trustee to apply the net income therefrom to the use of his wife during her life or until her remarriage. Upon the termination of the life estate, the trust was directed to be divided and continued upon certain shares for the benefit of a nephew and niece of the testator, with remainders over.

At the time of his death in 1934, the testator's residuary estate included, among various other assets, certain wholly owned guaranteed mortgages. Nine of these mortgages went into default after the death of the testator, and the estate acquired title to the real properties either by foreclosure or by deed in lieu of foreclosure prior to April 13, 1940; two of the properties were sold before that date, the income and proceeds therefrom, however, being retained in the hands of the trustee.

In the present proceeding the special guardian for the infant remaindermen contends, first, that the entire subdivision 2 of section 17-c is unconstitutional because it is expressly made retroactive in operation, and that, second, if constitutional, it does not apply, as a matter of construction, to the proceeds of the two properties which were sold before the statute became effective. The learned Surrogate sustained the constitutionality of the statute, but held as a matter of construction that it applied only to salvage operations uncompleted at the date of its enactment and hence was inapplicable to the two properties sold before it became effective. Upon appeal, the Appellate Division unanimously affirmed.

When a mortgage in default is foreclosed and title to the property is acquired by the trustee, the original mortgage investment is at an end and a salvage operation is initiated. (*Matter of Otis*, 276 N. Y. 101, 111, 112.) The real property thus acquired is substituted for the mortgage in the hands of the trustee and takes on the character of personalty.



(*Lockman v. Reilly*, 95 N. Y. 64, 71.) The trustee holds this real property so acquired and must administer it as an asset of the trust estate for the benefit of the life tenant and the remaindermen. Like the mortgage, it is "security not for principal alone but for income as well." (*Matter of Chapal*, 269 N. Y. 464, 472.) With respect to the mortgages which the testator owned at the time of his death and with respect to any real property which might be acquired by the trustee following default in any of these mortgages, the testator as creator of the trust gave no express directions except the general direction of what is commonly understood by the use of the words "income" and "principal." After the initiation of the salvage operation, as before, both the life tenant and the remaindermen could compel the trustee to administer the trust and to apportion to each his just share of the income and principal, but not that of any particular asset of the trust. (*Lockman v. Reilly*, 95 N. Y. 64, 71; *Bennett v. Garlock*, 79 N. Y. 302, 320.) Although the rule requiring apportionment as between income and principal, [fol. 254] of the proceeds of such sale has been long established (*Meldou v. Devlin*, 31 App. Div. 146; *affd.*, 167 N. Y. 573), the rules relating specifically to mortgage salvage operations were speeded in the process of formulation by the courts with the coming of the economic depression of the 1930's. In *Matter of Chapal* (269 N. Y. 464) this court said: "We have another problem—that of the liquidation of real estate acquired of necessity because of default on a mortgage investment." Concerning these rules thus worked out to meet the emergency resulting from widespread foreclosures, in *Matter of Otis*, *supra*, at page 112, we said: "Both capital account and income account, as described in the *Chapal* case, are fictions \* \* \*. If, then, the remaindermen are to participate in the apportionment on the feigned basis of unimpaired principal, the share of the life tenant should be computed on the same assumption. The invention of the 'original investment' is no more valid than the invention of 'unpaid interest' thereon. Indulgence in both fictions keeps the balance even between the respective parties in interest."

Moreover, we expressly said in the *Otis* case that the rules laid down were tentative only and not intended to be final. At page 115 it was said: "Perhaps it should be added that a general rule for such situations cannot be attained at a bound, that no rule can be final for all cases



and that any rule must in the end be shaped by considerations of business policy. Accordingly, we have here put aside inadequate legal analogies in the endeavor to express fair, convenient, practical guides that will be largely automatic in their application. Only the sure result of time will tell how far we have succeeded." It was also carefully pointed out that no hard and fast rule was laid down to guide the trustee in the disposition of net income earned during the salvage operation, but the disbursement of net income to the life beneficiary was left to the discretion of the trustee. In the *Otis* case we said at page 115: " \* \* \* the trustee may distribute such surplus income in its discretion. (269 N. Y. at p. 470). This discretion, moreover, should be exercised with appropriate regard for the fact that unless a life tenant gets cash he does not get anything in the here and now."

The Legislature has found, however, that trustees through fear of surcharge have accumulated surplus with the result that undue hardship has been visited upon life beneficiaries. Taking heed of this hardship at the request of the executive committee of the Surrogate's Association of the State of New York, the Legislature has declared its purposes in the statute itself. In part it reads: "The purpose of the enactment of this subdivision is declared to be the simplification of the rules of procedure in mortgage salvage operations and the elimination of present complications which work to the disadvantage of the life tenant \* \* \* by depriving him of a fixed right to the actual payment of any net income earned by the property. Such fixed right is granted in lieu of the discretion now given to the trustee to pay net income or any part thereof to the life tenant. \* \* \* Only equitable adjustments and balances as between the parties are intended to be effectuated by the provisions of this subdivision." Thus the Legislature has substituted in place of the discretion in the trustee permitting disbursement of surplus income, another more definite rule requiring some, albeit modest, payment of surplus income to the life beneficiaries. At the same time the Legislature has provided that additional income over and above the modest rate of payment shall be held until final adjustment, thus providing for equitable adjustments and balances as between life beneficiaries and remaindermen upon final liquidation, and safeguarding, so far as reasonably possible, the rights of all interested parties.

The statute provides: "Any payment of net income heretofore or hereafter made to the life tenant up to such three per centum per annum shall be final and shall not be subject to recoupment from the life tenant or as a surcharge against the trustee or executor. The amount of all such payments shall be taken into account, however, in the apportionment of the proceeds of sale and shall be charged against the share of the life tenant.

In thus formulating a rule that is final against recoupment for distribution of income received in excess of carrying charges, it does not appear that the Legislature has done more than direct a trustee to do what under the decisions of this court he has discretionary power to do. (*Matter of Otis, supra.*) Before the enactment of this statute, the life tenant could not have demanded as of right the payment to him during liquidation of more of the surplus income than he will receive under the statute. Neither does it appear that the remaindermen could properly have insisted that the trustee should be surcharged if in the exercise of his discretion he had paid to the life tenant the amount which the statute now directs. A statutory rule of administration which requires the trustee to apportion income in accordance with a fixed standard which in the exercise of administrative discretion the trustee would even without the statute have power to adopt does not, in our opinion, constitute a taking of property. The principle is applicable that "The mere fact that the statute is retroactive does not bring it in conflict with the Federal Constitution. \* \* \* Nor has a person a vested interest in any rule of law entitling him to have the rule remain unaltered." (*Preston Co. v. Funkhouser*, 261 N. Y. 140, 144; *Munn v. Illinois*, 94 U. S. 113.)

As already noted, the rules of administration heretofore set forth were tentatively stated and expressly recognized as subject to change. Before a judicial declaration, thus tentatively stated, becomes a rule of property, it must have become permanently fixed and long continued. (*United States v. Standard Oil*, 20 Fed. Supp. 427, 458; *affd.*, 107 F. [2d] 402, *cert. den.* 309 U. S. 673.) In that case the court said: "However, before setting up a judicial declaration as a rule of property, we should require, at least, that it be fixed, long-continued, and relied upon by persons acquiring property, so that its repudiation would amount to a denial of due process." Nor can the statute in the case

[fol. 256] at bar be said to be arbitrary or capricious, but on the contrary, it is fair and reasonable and protects the interest of both income beneficiaries and remaindermen. As was said in *Thompson v. Siratt* (95 F. [2d] 214, 217): "To hold that subsection (n) is repugnant to the Fifth Amendment requires a finding that its provisions are arbitrary and unreasonable."

We have, therefore, in the case at bar, no taking of property, no contract right involved and no impairment of due process. This statute, therefore, cannot be held to be unconstitutional. (*Robertson v. deBrulatour*, 188 N. Y. 301; *Brearley School, Ltd., v. Ward*, 201 N. Y. 358.)

The sole remaining question is whether or not the statute is applicable in cases where the liquidation was complete before the date when the statute became effective, the income and proceeds of property being still undistributed in the hands of the trustee. We concur in the construction placed upon the statute by the learned Surrogate, namely, that its scope is limited to cases where liquidation of real property acquired is incomplete. This is in accord with the language of the statute which provides that net income "during the salvage operation" shall be paid to the life tenant. Even in a "pending proceeding" or "action for an accounting," the language of the statute confines its application to cases where liquidation is incomplete and where "during the salvage operation" a trustee has acted in accordance with the discretion at that time invested in him. The apportionment of the proceeds of the property, both income and principal, where liquidation was completed before the statute became effective must be determined in accordance with the rules heretofore formulated by the court.

The order should be affirmed, with costs payable to the respondent trustee and one bill of costs to the infant appellants, William J. Demorest, Jr., Ann Demorest and Charles Demorest, payable out of the fund.

#### DISSENTING OPINION

LEWIS, J. (dissenting):

The infant-appellants, by their special guardian, challenge the constitutionality of section 17-c, subdivision 2, of the Personal Property Law (Cons. Laws, ch. 41). The problem relates to the apportionment, between an income

beneficiary and remaindermen, of income realized by a trustee from operations undertaken to salvage defaulted mortgages held by it as fiduciary. In this instance the mortgages in default were nine in number. The title to each mortgaged property came into the trustee either by foreclosure or by deed in lieu of foreclosure prior to April 13, 1940. Two of the properties were sold prior to that date, the avails of the sale being retained by the trustee.

The date last mentioned is important to our inquiry because it fixes the time when there became effective chapter 452 of the Laws of 1940 which added section 17-c to the Personal Property Law. It is the effect upon the rights of a life tenant and remaindermen of the retroactive provisions of subdivision 2 of that statute which has prompted the present challenge to its constitutionality.

Section 17-c of the Personal Property Law (added by L. 1940, ch. 452, effective April 13, 1940) provides rules for the administration of that portion of a trust fund in which is a [§ 257] real estate mortgage, held for the benefit of one or more tenants for life or a limited term with remainder over, where title to the mortgaged property has been acquired by the trustee by foreclosure or by conveyance in lieu of foreclosure. We are not here concerned with subdivision 1 of section 17-c which applies only to estates of persons dying, or trusts created, *after* its enactment and to mortgage investments made thereafter by a trustee of an existing trust. The challenge is to the constitutionality of subdivision 2 of section 17-c, the terms and rules of which "apply specifically (a) to the estates of persons dying *before* its enactment and (b) to mortgages on real property held by a trustee under a deed of trust or other instrument executed *before* the date of its enactment and (c) to real property acquired by foreclosure of mortgage or real property acquired in lieu of foreclosure *before* or after the date of its enactment in trusts created or mortgage investments made prior thereto . . . ." (Emphasis supplied.) In particular our inquiry goes to that portion of section 17-c to be found in subdivision 2 (a) which in general provides that, "regardless of advances made from the principal of a trust for the expense of a foreclosure, or of a conveyance of mortgaged property in lieu of foreclosure, and regardless of the cost of all capital improvements, payments—not subject to recoupment—shall be made to the life tenant from

the net income during the salvage operation up to three per cent per annum computed upon the principal amount of the mortgage.

Clearly subdivision 2 of section 17-c is retroactive. By its terms it presumes to affect acts which occurred, and rights which accrued, prior to April 13, 1940—the effective date of the statute. Among acts thus affected was the execution on December 14, 1928, of the testamentary trust here involved; among rights thus affected are those of the life tenant and the remaindermen in the proceeds from transactions undertaken by the trustee as a means of salvaging mortgages which were a part of that trust—mortgages which, as we have said, were “security not for principal alone but for income as well.” (*Matter of Chapal*, 269 N. Y. 464, 472.)

In the case last cited this court ruled that, upon a sale had in the course of a similar salvage operation (p. 472)—  
 “\* \* \* the proceeds should be used first to pay the expenses of the sale and the foreclosure costs and next to reimburse the capital account for any advances of capital for carrying charges not theretofore reimbursed out of income from the property. Then the balance is to be apportioned between principal and income in the proportion fixed by the respective amounts thereof represented by the net sale proceeds. In the capital account will be the original mortgage investment. In the income account will be unpaid interest accrued to the date of sale upon the original capital.”  
 (And see *Matter of Otis*, 276 N. Y. 101, 111; *Matter of McManis*, 282 N. Y. 420, 425.)

When the properties here involved came into the hands of the trustee, the rule of apportionment last quoted above was not a matter of grace as the majority opinion herein [fol. 258] seems to hold. It was a rule of property the essential principle of which had long been recognized and applied in this jurisdiction and others, including England. (*Meldon v. Dertin*, 31 App. Div. 146; *affd.*, 167 N. Y. 573 [1901]; *Pursons v. Winslow*, 16 Mass. 361, 365 [1820]; *Veazie v. Forsaith*, 76 Me. 172 [1884]; *Hagan v. Platt*, 48 N. J. Eq. 206, 207, 208 [1891]; *Greene v. Greene*, 19 R. I. 619, 621-624 [1896]; *Quinn v. First Nat. Bank*, 168 Tenn. 30 [1934]; *Matter of Nirdlinger*, 327 Penn. St. 171, 172, 173 [1937]; *Cox v. Cox*, L. R. 8 Eq. 343, 344, 345 [1869]; *Matter of Moore*, 54 L. J. Ch. 432 [1885], and see *Matter of Mar-*



shall, 43 Misc. Rep. 238, 245 [1904].) A classical statement of the underlying principle which runs through the cases cited above was made in *Cox v. Cox*, *supra*, page 344 as follows: "The true principle in all these cases is, that neither the tenant for life nor the remainderman is to gain an advantage over the other—neither is to suffer more damage in proportion to his estate and interest than the other suffers—from the default of the obligor." (Emphasis supplied.) This was orthodox doctrine long before the decisions by this court in the *Meldon*, *Chapal* and *Otis* cases, *supra*.

In accord with that rule of property there had vested in the income beneficiary and the remaindermen respectively, prior to the effective date of section 17-c, subdivision 2, a proprietary interest in each of the properties acquired by the trustee. (*Matter of McManus*, *supra*, p. 426.)

Although the basis adopted by the courts for computing the item of interest involved differs in the various jurisdictions which have considered the question, there is a basic principle, as we have seen, which runs throughout the decisions cited above—*viz.*, that, in the proceeds from salvage operations incidental to the administration of a trust estate, both life tenant and remainderman have a proprietary interest and both are entitled to be paid their proportionate shares thereof.

The comment made in *Matter of Rogers* (22 App. Div. 428; *affd.*, 161 N. Y. 108), by Mr. Justice Cullen—later Chief Judge of this court—applies with equal force in the case at hand where the rights of remaindermen are at stake (p. 436)—"The equities of a life tenant to receive the whole income that may accrue during his tenancy are every whit as great as that of the remaindermen to have the corpus of the trust preserved unimpaired. \* \* \* Why should each not have exactly his own, so far as it is possible to ascertain it?" (Emphasis supplied.)

A marked difference should be noted between the provisions of section 17-c, subdivision 2, with which we are here concerned, and subdivision 1 of the same section. Unlike subdivision 2, the Legislature was careful in subdivision 1 to make its mandates in effect prospective—not retroactive. It also employed language by which its mandates would in no event conflict with any contrary intention which might be expressed by the creator of the trust.



[fol. 259] The resultant effect of section 17-c, subdivision 2, is to transfer, without the right of recoupment, from the principal account of a trust to the income account, an amount—fixed arbitrarily and without regard to the demands of justice and equity in the circumstances at three per cent per annum computed upon the principal amount of each salvaged mortgage. Such a mandatory transfer to the life tenant of property rights which had become vested in the remaindermen under a rule of property which antedated the enactment of section 17-c, subdivision 2, transcends the Legislature's power. "Legislation which impairs the value of a vested estate is unconstitutional." (*Matter of Pell*, 171 N. Y. 48, 52, 53; *People v. O'Brien*, 111 N. Y. 1, 57-59; *Westervelt v. Gregg*, 12 N. Y. 202, 212.) As I view the statute it authorizes, without due process of law, the taking of property rights which became vested in the remaindermen under an established rule of property prior to the effective date of the statute. To that extent it violates the Fourteenth amendment to the Federal Constitution and article 1, section 6, of the Constitution of the State of New York.

I pass now to a phase of the problem which I think cannot be ignored. The questions of apportionment with which subdivision 2 of the statute attempts to deal are essentially judicial questions. This subject was examined by Story in his *Equity Jurisprudence* ([2d ed.] vol. 1, § 489 *et seq.*) Stressing the "beneficial operations of courts of equity . . . upon this confessedly intricate subject," he said: "Without some proceedings, in the nature of an account before a Master, there would be no suitable elements upon which any court of justice could dispose of the merits of such cases." In like vein it was said by Judge Loughran writing for this court in *Matter of Otis*, *supra* (p. 115), that . . . a general rule for such situations cannot be attained at a bound, that *no rule can be final for all cases* and that any rule must in the end be shaped by considerations of business policy." Subdivision 2 of the statute attempts to override all this by saying that *in every case* the life tenant must at all events immediately and finally receive net income at a rate arbitrarily fixed by the statute at three per cent—no matter what may be the cross-equities of the parties and without regard for the business risks of the particular salvage operations. To this extent, subdivision 2 of the statute makes it mandatory that the court

shall adjudicate every "pending proceeding, or action for an accounting" without affording the parties any opportunity to be heard. The draftsmen of the statute apparently recognized some difficulty on that score, for the statute says: "Only equitable adjustments and balances, *as between the parties* are intended to be effectuated by the provisions of this subdivision" [2]. (Emphasis supplied.)

We have, then, this extraordinary situation: While subdivision 2 of the statute has not changed the law that pending questions of apportionment are to be decided upon equitable principles, yet it declares that such principles must be applied by the courts, not according to the judicial judgment of what is equitable in the circumstances of a pending controversy, but according to a legislative mandate rigidly enjoined for all pending cases.

[fol. 260]. The Legislature has no power so to declare the law "for the information and government of the courts in the decision of causes before them." (Kent, Ch. J., in *Dash v. Van Kleeck*, 7 Johns. 477, 508, 509.) In this connection it should be observed that subdivision 2 of the statute is not emergency legislation; it invokes neither the general welfare nor any other consideration of public policy. In the only opinion written below, it is said: "The Legislature has done no more in formulating a modification of existing rules than the courts themselves could do. \* \* \*." (175 Misc. 1044, at p. 1050.) Such a proposition is not free from risk. Nobody knows what economic chaos may follow the present war. I am not prepared to say that as to all pending cases the Legislature may do at one stroke whatever courts of justice may do in accord with their tradition to proceed only in a particular controversy and only after taking evidence at a hearing held upon issues defined by pleadings. The Legislature can no more exercise judicial power than our courts can exercise legislative power. (See opinion by Ruffin, C. J., in *Hoke v. Henderson*, 25 Amer. Dec. p. 686 [N. C.].) The determination of rights of property *inter partes* is always a judicial question. As I view it, subdivision 2 of section 17-c of the Personal Property Law is a void attempt by the Legislature to make such a determination.

I am led by these considerations to dissent and vote for a modification of the Surrogate's decree accordingly.

## DISSENTING OPINION

Loughran, J. (dissenting). I add a few words to the dissenting opinion of Judge Lewis in which I concur entirely.

The crux of the prevailing opinion is this striking sentence: "A statutory rule of administration which requires the trustee to apportion income in accordance with a fixed standard which in the exercise of administrative discretion the trustee would even without the statute have power to adopt does not, in our opinion, constitute a taking of property." I cannot assent to so free an appraisal of the retroactive mandate of the Legislature.

No authority is cited to show that it was always open to trustees of their own motion to pay net income to a life tenant at such a "fixed standard," in peremptory disregard of the recoupment rights of remaindermen. Indeed, the general understanding of the profession appears to have been the other way, seeing that the Surrogates who devised the statute have vouchsafed us one reason alone for its enactment, *viz.*, "Trustees have hesitated to pay such net income because in the case of overpayment to the life tenant, the trustee might be surcharged with that amount." (See L. 1940, p. 1182.)

This recognition by trustees of the conflicting rights of remaindermen was not without justification. It is true that hitherto a trustee for a life tenant and remaindermen was entitled to distribute surplus income in his discretion. (*Matter of Otis*, 276 N. Y. 101, 115.) But that discretion was always to be exercised by a trustee with reasonable judgment and with an even hand between the life tenant [fol. 261] and the remaindermen in the particular circumstances. (*See Carrier v. Carrier*, 226 N. Y. 114, 125, 126; 28 Halsbury's Laws of England, (1st ed.) 123, 124; 2 Scott on The Law of Trusts, § 187; 4 Pomeroy on Equity Jurisprudence, [5th ed.] § 1062a.) The retroactive provisions of the statute direct trustees instantaneously to make final payment of net income to a life tenant not at a fixed rate merely, but at the expense of the remaindermen if need be. Hence I cannot accept the presupposition that the statute confers no new power upon trustees.

There is no occasion now for examination of the real nature of the equitable right of a trust beneficiary. At least the beneficiary owns the obligation of the trustee—

a thing which is as truly the subject-matter of property as any physical object. (See Ames, Lectures on Legal History, p. 262. Cf. 1 Scott on The Law of Trusts, § 130.) Consequently I see no warrant for the view that the respective interests of beneficiaries of a discretionary trust are not rights of property in the constitutional sense. (See *Pritchard v. Norton*, 106 U. S. 124, 132.)

Lehman, Ch. J., Rippey, Conway and Desmond, JJ., concur with Finch, J.; Lewis and Loughran, JJ., dissent in separate opinions in which both concur.

Order affirmed, etc.

[fol. 262] IN COURT OF APPEALS OF NEW YORK

STATE OF NEW YORK, ss:

Pleas in the Court of Appeals, held at Court of Appeals Hall in the City of Albany, on the 14th day of January, in the year of our Lord one thousand nine hundred and forty-three, before the Judges of said Court.

Witness, The Hon. Irving Lehman, Chief Judge, Presiding. John Ludden, Clerk.

In the Matter of the Judicial Settlement, &c., of City Bank Farmers Trust Company, as Trustee &c., Last Will &c., of Henry C. West, dec'd., &c.

REMITTITUR—January 15, 1943.

Be It Remembered, That on the 15th day of May in the year of our Lord one thousand nine hundred and forty-two Emma M. West and others &c., the appellants in this cause, came here unto the Court of Appeals, by Larkin, Rathbone & Perry, and another, their attorneys, and filed in the said Court Notices of Appeal and return thereto from the order of the Appellate Division of the Supreme Court in and for the First Judicial Department. And City Bank Farmers Trust Company, as Trustee &c., and others, the respondents in said cause, afterwards appeared in said Court of Appeals by Mitchell, Taylor, Capron & Marsh and others, their attorneys.

Which said Notices of Appeal and the return thereto, [fols. 263-267] filed as aforesaid, are hereunto annexed.

Whereupon, The said Court of Appeals having heard this cause argued by Mr. Francis J. Mahoney of counsel for the appellants, Mr. Albert Stickney for appellant-respondent West; by Mr. C. Alexander Capron of counsel for the respondent-trustee, and after due deliberation had thereon, did order and adjudge that the order of the Appellate Division of the Supreme Court appealed from herein be and the same hereby is affirmed, with costs to the respondent trustee and one bill of costs to the infant appellants, William J. Demorest, Jr., Ann Demorest and Charles Demorest, payable out of the fund.

And it was also further ordered, that the record aforesaid, and the proceedings in this Court, be remitted to the Surrogates' Court, New York County, there to be proceeded upon according to law.

Therefore, it is considered that the said order be affirmed, with costs, &c., as aforesaid.

And hereupon, as well the Notices of Appeal and return thereto aforesaid as the judgment of the Court of Appeals aforesaid, by it given in the premises, are by the said Court of Appeals remitted into the Surrogates' Court, New York County, before the Surrogates thereof, according to the form of the statute in such case made and provided, to be enforced according to law, and which record now remains in the said Surrogates' Court before the Surrogates thereof, &c.

John Ludden, Clerk of the Court of Appeals of the State of New York.

Court of Appeals, Clerk's Office,  
Albany, January 15, 1943.

I Hereby Certify, that the preceding record contains a correct transcript of the proceedings in said cause in the Court of Appeals, with the papers originally filed therein, attached thereto.

John Ludden, Clerk. (Seal.)

STATE OF NEW YORK,

County of New York, ss.:

I, George Loesch, Clerk of the Surrogate's Court of said County, do hereby certify that I have compared the foregoing copy of Remittitur from Court of Appeals, in the matter of the estate of Henry C. West, deceased, Filed

January 25, 1943, with the original record thereof now remaining in this office, and have found the same to be a correct transcript therefrom and of the whole of such original record.

In testimony whereof, I have hereunto set my hand and affixed the seal of the Surrogate's Court of the County of New York this 3rd day of May in the year of our Lord one thousand nine hundred and forty-three.

George Loesch, Clerk of the Surrogate's Court.

P-1379-1934. McG/S.

[fol. 268] IN COURT OF APPEALS OF THE STATE OF NEW YORK

[Title omitted]

PETITION FOR APPEAL FROM THE COURT OF APPEALS OF STATE OF NEW YORK TO THE SUPREME COURT OF THE UNITED STATES

To the Honorable Irving Lehman, Chief Judge of the Court of Appeals of the State of New York:

William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, by Gerald P. Culkin, as special guardian, your [fol. 269] petitioners, respectfully show:

1. Petitioners are appellants in the above entitled cause.
2. The above named respondent, City Bank Farmers Trust Company, as trustee of the trusts created under the last will and testament of Henry C. West, deceased, on or about the 2nd day of December, 1940, filed in the Surrogate's Court, New York County, State of New York, its account of proceedings as trustee as aforesaid, together with its petition praying for the judicial settlement of its account of proceedings as trustee as aforesaid, and for a judicial construction of said will and instructions and directions.

3. In the proceeding so instituted, your petitioners, by the report and objections of Gerald P. Culkin, as special guardian as aforesaid, asserted the invalidity of subdivision 2 of Section 17-c of the Personal Property Law of the State of New York (Chapter 452 of the Laws of 1940, effective April 13, 1940), on the ground that it was repugnant to



the Fourteenth Amendment to the Constitution of the United States of America, because it deprived his wards as remaindermen of the trust estate of their property without due process of law.

4. By its decree dated September 8, 1941 and entered in the office of the Clerk of the Surrogate's Court of the County of New York on September 9, 1941, said Court sustained the validity of said subdivision 2 of Section 17-c of the Personal Property Law and overruled the contentions [fol. 270] and objections of your petitioners, which were based upon the claimed unconstitutionality of said statute. In and by said decree it was provided that the account of the trustee as aforesaid be settled upon the basis that said subdivision 2 of Section 17-c of the Personal Property Law was constitutional, and the trustee was thereby instructed and directed to govern its conduct as such trustee in the future on the basis that said statute was constitutional.

5. Your petitioners appealed from said decree of said Surrogate's Court to the Appellate Division of the Supreme Court of the State of New York, held in and for the First Judicial Department, which said Appellate Division thereafter unanimously affirmed said decree by its order bearing date and made and entered on the 2nd day of April, 1942, and in and by said order of April 2, 1942 as the same was resettled by the order of said Court bearing date and made and entered April 16, 1942.

6. Your petitioners thereupon appealed to the Court of Appeals of the State of New York from said order, as resettled, in so far as the same sustained the constitutionality of Section 17-c, subdivision 2 of the Personal Property Law of the State of New York.

7. The said Court of Appeals on the 15th day of January, 1943, two judges dissenting, made its final judgment wherein and whereby it was ordered and adjudged that said order of the Appellate Division of the Supreme Court of the State of New York should be affirmed, and on or about the 25th [fol. 271] day of January, 1943, the remittitur of said Court of Appeals, with the record in the said case was filed in the office of the Clerk of the Surrogate's Court, New York County, in accordance with law, and there remains, and by order dated the 5th day of March, 1943, and entered the 6th day of March, 1943, of said Surrogate's Court, the said

order of said Appellate Division and the said judgment of said Court of Appeals were thereby made the orders of said Surrogate's Court.

8. The said Court of Appeals of the State of New York is the highest court of the State of New York in which a decision in this suit could be had.

9. As above stated, in said suit there is drawn in question the validity of a statute of the State of New York, namely, subdivision 2, of Section 17-c of the Personal Property Law, Chapter 452 of the Laws of New York (1940), on the ground that it is repugnant to the Fourteenth Amendment to the Constitution of the United States of America, and the decision and final judgment of the Court of Appeals of the State of New York is in favor of the validity of said statute.

10. In said decision and final judgment certain errors were committed to the prejudice of petitioners which are more fully set forth in the assignment of errors filed herewith.

Wherefore, petitioners pray for the allowance of an appeal from said Court of Appeals of the State of New York, [fol. 272] to the Supreme Court of the United States, in order that the decision and final judgment of the Court of Appeals of the State of New York herein may be affirmed and reversed, and also prays that a transcript of the records, proceedings and papers in this case, duly authenticated by the Clerk of the Surrogate's Court of New York County, State of New York, may be sent to the Supreme Court of the United States, as provided by law.

Dated: New York, N. Y., April 2nd, 1943.

Gerald P. Culkin, Special Guardian for William J. Demorest, Jr., Ann Demorest and Carolyn Demorest.

[fol. 273] IN COURT OF APPEALS OF THE STATE OF NEW YORK

[Title omitted]

#### ASSIGNMENT OF ERRORS

Now comes William J. Demorest, Jr., Ann Demorest and Carolyn Demorest by their Special Guardian, Gerald P. Culkin, the appellants herein to the Supreme Court of

the United States from the judgment and decision of the [fol. 274] Court of Appeals of the State of New York, and assign as errors the following holdings of said Court of Appeals:

(1) Section 17-c of the Personal Property Law of the State of New York (Chap. 452 of the Laws of New York 1940) as applied to the trust created under the Will of Henry C. West and to its administration, was not repugnant to the Fourteenth Amendment to the Constitution of the United States.

(2) Said statute did not deprive appellants of their property without due process of law in violation of the Fourteenth Amendment to the Constitution of the United States, although, said statute required the trustee under the will of Henry C. West, who died prior to the enactment of said statute, to pay to the life beneficiary of said trust rents from real properties acquired in an attempt to salvage the investment in mortgages thereon theretofore held by said trustee, which rents under the law of the State of New York, existing prior to the enactment of said statute, constituted principal of said trust in which appellants are interested as remaindermen.

(3) Said statute, as applied to mortgages acquired by the trustee of said trust prior to the enactment of said statute, did not violate the rights guaranteed to appellants by said Fourteenth Amendment.

(4) Said statute as applied to rents received, prior to the enactment of said statute, from real property acquired by said trustee in an attempt to salvage investments in mortgages thereon held by said trustee, did not violate the rights guaranteed to appellants by said Fourteenth Amendment,

[fol. 275] (5) Said statute did not violate the rights guaranteed appellants by said Fourteenth Amendment, although it required said trustee, if and when it received from such a parcel of real property during any year, income in excess of expenses of operating said parcel during said year, to pay to the life beneficiary of said trust such excess income for such year, to the extent of three per cent of the principal of the mortgage, although such parcel earned no net income for the whole period from its acquisition by the trustee to the end of such year, and moneys constituting principal of

said trust had been used for the payment of operating expenses of said parcel in prior years.

(6) Said statute did not violate the rights guaranteed to appellants by the Fourteenth Amendment, although, pursuant thereto, the trustee was required to distribute as income certain of the rents which might thereafter be collected from said parcels of real property or from any other parcel of real property which might be acquired on the foreclosure, or by deed in lieu of foreclosure, of a mortgage which was held by the trustee at the time of the enactment of said statute.

Dated: April 2nd, 1943.

Gerald P. Culkin, Special Guardian for William J. Demorest, Jr., Ann Demorest and Carolyn Demorest.

[fol. 276] IN THE COURT OF APPEALS OF THE STATE OF NEW YORK

[Title omitted]

#### ORDER ALLOWING APPEAL

Upon the petition of William J. Demorest, Jr., Ann Demorest and Carolyn Demorest by their special guardian, Gerald P. Culkin, dated the 2nd day of April, 1943, for an appeal in the above cause to the Supreme Court of the United States from the Court of Appeals of the State of New York, and their assignment of errors and jurisdictional [fol. 277] statement pursuant to Rule 12 of the Rules of the Supreme Court of the United States; and it appearing therefrom and from the records of the above-entitled cause that there was drawn in question in said cause the validity of a statute of the State of New York on the ground that it is repugnant to the Fourteenth Amendment to the Constitution of the United States and that the decision and final judgment of the Court of Appeals is in favor of the validity of said statute;

Now, Therefore, it is

Ordered that said appeal be and the same hereby is allowed as prayed in the petition and that the Clerk of the Surrogate's Court, New York County, State of New York,

shall prepare and certify a transcript of the records and proceedings in the above cause and transmit the same to the Supreme Court of the United States within thirty (30) days from the date hereof; and it is

Further Ordered that the appellants shall give good and sufficient security in the sum of \$500, to be approved by the undersigned, that said appellants shall prosecute said appeal to effect and if said appellants fail to make their plea good they shall answer all costs.

Dated: April 3d, 1943.

Irving Lehman, Chief Judge of the Court of Appeals of the State of New York.

[fols. 278-285] Citation in usual form showing service on Appellees, omitted in printing.

[fol. 286] SUPREME COURT OF THE UNITED STATES

STATEMENT AND DESIGNATION PURSUANT TO PARAGRAPH 9 OF RULE 13 OF THE RULES OF THE SUPREME COURT OF THE UNITED STATES—Filed April 26, 1943

Now comes William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, by Gerald P. Culkin, Special Guardian, and for a definite statement of the points upon which they intend to rely on this appeal, pursuant to paragraph 9 of Rule 13 of the Rules of the Supreme Court of the United States, adopt their assignment of errors herein bearing date April 2, 1943; and do hereby designate as the parts of the Record which they think necessary for the consideration thereof by this Court, which are fully set forth in the designation hereto annexed.

Gerald P. Culkin, Special Guardian for Infant Appellants.

Due and timely service of the foregoing statement and designation is hereby admitted, this 23rd day of April, 1943.

[fol. 287] C. Alexander Capron, Charles Anzulo, Attorneys for City Bank Farmers Trust Company, as trustee, appellee. Albert Stickney, Attorney for Emma M. West, appellee. James Morrow, Attorney for Marie Elizabeth West Jones and Elizabeth Frances Jones, appellees.

## [fol. 288] SUPREME COURT OF THE UNITED STATES

DESIGNATION PURSUANT TO PARAGRAPH 9 OF RULE 13 OF THE  
RULES OF THE SUPREME COURT OF THE UNITED STATES

The parties hereto by their undersigned counsel do hereby, pursuant to the provisions of paragraph 9 of Rule 13 of the Rules of the Supreme Court of the United States, designate the parts of the Record which they respectively think necessary for the consideration thereof by this Court, as follows:

(1) opinion of the Court of Appeals of the State of New York;

(2) remittitur of the Court of Appeals of the State of New York;

(3) petition for appeal;

(4) assignment of errors;

(5) order allowing appeal;

(6) citation on appeal; and

(7) the following portions of the Record on Appeal:

(a) notice of appeal of infant appellants to Appellate Division (fols. 10-17);

(b) decree construing will and settling account (fols. 31-135);

[fol. 289] (c) petition for judicial settlement of trustee's account, etc. (fols. 142-188);

(d) excerpts from intermediate account of trustee's proceedings (fols. 190-399) (with deletions as noted upon the annexed copy of said Record on Appeal);

(e) report and objections of special guardian (fols. 400-477) (excluding Schedule A thereto annexed);

(f) will of Henry C. West (fols. 577-591);

(g) opinion of Surrogate, dated March 8, 1941 (fols. 604-684);

(h) notice of appeal to Court of Appeals of infant appellants (fols. 703-708);



(i) order of Appellate Division of affirmance as resettled on April 16, 1942 (fols. 733-744).

Dated: New York, N. Y., April 23rd, 1943.

Gerald P. Culkin, Special Guardian for Infant Appellants; C. Alexander Capron, Charles Anzulo, Attorneys for City Bank Farmers Trust Company, as Trustee, Appellee; Albert Stickney, Attorney for Emma M. West, Appellee; James Morrow, Attorney for Marie Elizabeth West Jones and Elizabeth Frances Jones, Appellees.

[fol. 289a] [File endorsement omitted.]

[fol. 290] SUPREME COURT OF THE UNITED STATES

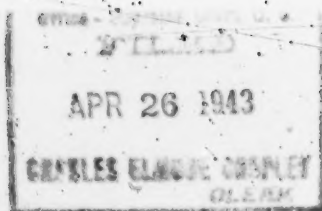
ORDER NOTING PROBABLE JURISDICTION—May 17, 1943

The statement of jurisdiction in this case having been submitted and considered by the Court, probable jurisdiction is noted.

Endorsed on Cover: File No. 47,458. New York, Surrogate's Court, New York County. Term No. 52. William J. Demorest, Jr., Ann Demorest and Carolyn Demorest by Gerald P. Culkin, Their Special Guardian, Appellants, vs. City Bank Farmers Trust Company, as Trustee under the will of Henry C. West, Deceased, et al. Filed April 26, 1943. Term No. 52 O. T. 1943.

(17541)

**FILE COPY**



**SUPREME COURT OF THE UNITED STATES**

**OCTOBER TERM, 1942**

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**No. 957 - 52**

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**WILLIAM J. DEMOREST, JR., ANN DEMOREST AND  
CAROLYN DEMOREST, BY GERALD P. CULKIN,  
THEIR SPECIAL GUARDIAN,**

*Appellants,*

*vs.*

**CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE  
UNDER THE WILL OF HENRY C. WEST, DECEASED, ET AL.**

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**APPEAL FROM THE SUBROGATE'S COURT OF NEW YORK COUNTY,  
STATE OF NEW YORK.**

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**STATEMENT AS TO JURISDICTION.**

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**GERALD P. CULKIN,**  
*Counsel for Appellants.*

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## COURT OF APPEALS OF THE STATE OF NEW YORK

In the Matter of the Judicial Settlement of the Account of Proceedings of CITY BANK FARMERS TRUST COMPANY as Trustee of the trusts created under the Last Will and Testament of HENRY C. WEST, Deceased, and of the Application of CITY BANK FARMERS TRUST COMPANY as Trustee as aforesaid, for a Determination as to the Construction and Effect of said testator's Last Will and Testament, and for Instructions and Directions as to the Manner and Method of Allocation and Distribution of the Funds which are now or may hereafter be in its hands as Trustee as aforesaid.

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WILLIAM J. DEMOREST, JR., ANN DEMOREST AND  
CAROLYN DEMOREST,

*Infant Appellants,*

EMMA M. WEST,

*Appellant,*

CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE,  
ETC.

*Respondent,*

MARIE ELIZABETH WEST JONES AND ELIZABETH  
FRANCES JONES,

*Respondents.*

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### JURISDICTIONAL STATEMENT PURSUANT TO SUPREME COURT RULE 12.

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Comes now William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, by their special guardian, Gerald P. Culkin, the appellants herein, and file the following state-

ment as required by Rule 12 of the Supreme Court of the United States.

**1. Basis Upon Which It Is Contended That the Supreme Court of the United States Has Jurisdiction.**

The judgment appealed from is the final judgment of the Court of Appeals of the State of New York, the highest court in the State of New York in which a decision herein could be had, and there is drawn in question in this suit the validity of a statute of the State of New York on the ground of its being repugnant to the Constitution of the United States and the said decision of said Court of Appeals is in favor of the validity of said statute.

**2. Statutory Provision Believed to Sustain Jurisdiction.**

The statutory provision which sustains the appellate jurisdiction herein of the Supreme Court of the United States is Section 237(a) of the Judicial Code, as amended by the Act of February 13, 1925, Chapter 229, 43 Stat. 936 [28 U. S. C. A. Sect. 344(a)]; also the Act of January 31, 1928, Chapter 14, Section 1, 45 Stat. 54 and the Act of April 26, 1928, Chapter 440, 45 Stat. 466 [28 U. S. C. A. Sect. 861a, 861b].

**3. The Statute of the State, the Validity of Which Is Involved.**

The statute of the State of New York herein involved is subdivision 2 of Section 17-c of the Personal Property Law of the State of New York which is a part of Chapter 452 of the Laws of New York 1940, p. 1182. Said statute became a law on April 13, 1940, with the approval of the Governor of the State of New York. Subdivision 2 thereof provides as follows:

“2. The existing rules of procedure applying to salvage operations respecting existing mortgage invest-



ments are continued except as modified by the subparagraphs hereinafter set forth. The terms and rules of procedure of this subdivision shall apply specifically (a) to the estates of persons dying before its enactment and (b) to mortgages on real property held by a trustee under a deed of trust or other instrument executed before the date of its enactment and (c) to real property acquired by foreclosure of mortgage or real property acquired in lieu of foreclosure before or after the date of its enactment in trusts created or mortgage investments made prior thereto, and (d) to any pending proceeding or action for an accounting of the transactions of an executor or trustee.

(a) Net income during the salvage operation up to three per centum per annum upon the principal amount of the mortgage shall be paid to the life tenant, regardless of principal advances for the expenses of foreclosure or of conveyance in lieu of foreclosure and arrears of taxes and other liens which occurred prior to such foreclosure or conveyance and the cost of all capital improvements. Any payment of net income heretofore or hereafter made to the life tenant up to such three per centum per annum shall be final and shall be not subject to recoupment from the life tenant or as a surcharge against the trustee or executor. The amount of all such payments shall be taken into account, however, in the apportionment of the proceeds of sale and shall be charged against the share of the life tenant.

(b) The foregoing principal advances shall be repaid out of excess net income above such three per centum per annum. When principal advances have been satisfied, any excess income shall be impounded (subject to reinvestment under the terms of the will or deed) to await sale and apportionment.

(c) The unpaid principal advances shall be a primary lien upon the proceeds of sale and shall be paid first out of any cash so derived. If insufficient the balance shall be a primary lien upon any purchase money mortgage received upon the sale.

(d) The purpose of the enactment of this subdivision is declared to be the simplification of the rules of procedure in mortgage salvage operations and the elimination of present complications which work to the disadvantage of the life tenant, who is usually the principal object of the testator's or settlor's bounty, by depriving him of a fixed right to the actual payment of any net income earned by the property. Such fixed right is granted in lieu of the discretion now given to the trustee to pay net income or any part thereof to the life tenant. The general rules of the apportionment of the proceeds of sale between life tenant and remainderman are retained subject to the express modifications made herein. Only equitable adjustments and balances as between the parties are intended to be effectuated by the provisions of this subdivision. If any provision of this subdivision or the application thereof to any mortgage or acquired property by foreclosure or conveyance, or to any trust is held invalid, the remainder of the subdivision and the application of such provision to any other mortgage or property acquired by foreclosure or conveyance or other trust shall not be affected thereby."

#### **4. Date of Judgment and Application for Appeal.**

The date of the judgment of the Court of Appeals of New York sought to be reviewed herein is January 15, 1942, and the same was entered pursuant to the provisions of the law of New York in the Surrogate's Court, New York County, State of New York, on the 25th day of January, 1943. The date upon which the application for appeal is presented is April 3rd, 1943.

#### **5. The Nature of the Case and of the Rulings of the State Court Which Bring the Case Within the Jurisdictional Provisions Relied On.**

This proceeding was instituted in the Surrogate's Court of New York County, State of New York, by City Bank

Farmers Trust Company, as trustee under the last will and testament of Henry C. West, deceased, who died on the 1st day of May, 1934, a resident of said county. In said proceeding the said trustee prayed for a judicial settlement of the account of its proceedings as trustee down to the 31st day of July, 1940, and for instructions and directions with respect to its administration of said trust after said date. A respondent in said proceeding, Emma M. West, was the life beneficiary of the trust created under said last will and testament and your appellants are remaindermen thereof. The principal of said trust estate was in large part composed of bonds and mortgages owned by decedent at the date of his death.

Prior to April 13, 1940, some of said mortgages were foreclosed by the trustee and the real property covered thereby acquired by the trustee upon foreclosure sales, and in other instances deeds in lieu of such foreclosure were accepted by the trustee.

On April 13, 1940, the Governor of the State of New York approved Chapter 452 of the Laws of New York, 1940, which became Section 17-c of the Personal Property Law of the State of New York, which statute changed and modified the rules theretofore existing in the State of New York with respect to payment to life beneficiaries of rents received from real property acquired in salvage of mortgage investments held by trustees, by directing that out of any net rents received from such a parcel in any year there should be paid to the life beneficiary, without any right of recoupment, an amount equal to 3% of the face amount of the mortgage covering the property so acquired.

The account of proceedings of said trustee was prepared and submitted upon the basis that subdivision 2 of section 17-c of the Personal Property Law of the State of New York applied to the transactions of said trustee prior to April 13, 1940, and by its petition the said trustee requested

that it be instructed as to whether said statute should govern its future administration of said trust estate.

Your appellants, by the report and objections to said account filed by their special guardian, took the position that said statute could not be applied to the account of proceedings so filed or to the future administration of said trust without depriving them of their property without due process of law contrary to the provisions of the Fourteenth Amendment to the Constitution of the United States.

The objections of your appellants were overruled by the decree of the Surrogate's Court and the trustee was directed to administer said trust on the basis that said statute was applicable to its actions subsequent to the date of said account. The decree of the Surrogate's Court was affirmed by order of the Appellate Division of the Supreme Court in and for the First Judicial Department of the State of New York to which an appeal was taken, and on further appeal to the Court of Appeals of the State of New York the order of the Appellate Division was affirmed. The final judgment of the Court of Appeals is, therefore, in favor of the validity of the state statute, against the contention of your appellants that said statute was invalid as repugnant to the Federal Constitution.

#### **6. Cases Believed to Sustain Jurisdiction.**

*Senn v. Tile Layers Union*, 301 U. S. 468, 476-7. There as here a state statute was involved, and the issue presented as to whether it violated the Fourteenth Amendment, which issue had never been passed upon by the United States Supreme Court. A motion to dismiss the appeal was denied.

#### **7. State of Proceedings in State Courts and Manner in Which Federal Questions Sought to Be Reviewed Were Raised.**

The account of proceedings of the trustee filed in the Surrogate's Court, New York County, State of New York,

was prepared on the basis that subdivision 2 of Section 17-c of the Personal Property Law applied to the allocation and apportionment of rents received from real property prior to the date of the enactment of such statute on April 13, 1940, and in its petition the trustee prayed for the judicial settlement of said account and requested instructions as to the manner in which moneys received by way of rents or proceeds of sale of real property acquired upon foreclosure of mortgage or by deed in lieu of foreclosure should be apportioned between principal and income of said trust estate subsequent to the closing date of said account (Record on Appeal—Petition: pp. 58-9, 61-2, fols. 174-7, 183-6; Account: 64-133, particularly income schedule p. 77, fols. 230-1, and recapitulations pp. 87-8, 92-3, 97-8, 102-3, 107-8, 113-14, 118-19).

At the first opportunity to do so your appellants, by the report and objections of their special guardian, raised the issue as to the unconstitutionality of subdivision 2 of Section 17-c of the Personal Property Law and asserted that it was repugnant to the Fourteenth Amendment to the Constitution of the United States, (Record on Appeal, p. 136, fol. 407, p. 139, fols. 416-17), objected to the allocation of income made on the basis of annual rents without regard to whether any net income had been derived from the property during the period of its operation on the ground that such method of computing annual income was unconstitutional (Record on Appeal, p. 136, fols. 407-8), objected to the items in which rents from said properties were credited to income (objections Numbered I and II, Record on Appeal, pp. 136-140, fols. 408-418). In support of said Objections it was stated (p. 139, fols. 416, 417):

“ \* \* \* said statute is invalid and unconstitutional and its provisions arbitrary and said statute deprives my wards as residuary remaindermen of the trust estate of property without due process of law and in a manner prohibited by and contrary to the provisions of



• • • of the 14th Amendment to the Constitution of the United States of America."

The decree of the Surrogate's Court in this proceeding overruled said objections numbered I and II of the special guardian for your appellants (Record on Appeal, p. 19, fol. 55), judicially settled and allowed the account of proceedings of said trustee as filed with adjustments not here material (Record on Appeal, pp. 29-30, 32; fols. 87-8, 95-6) and gave extensive instructions to said trustee as to the manner of keeping its accounts and allocating as between principal and income the proceeds of sale and rents which might be received after the closing date of said account from property acquired by it upon foreclosure of mortgages held by it as such trustee or by deed in lieu of foreclosure thereof (said mortgages having been acquired prior to the date of the enactment of said statute), on the basis that subdivision 2 of Section 17-c applied to govern said trust and was constitutional in such application (Record on Appeal, pp. 32-43, fols. 96-127).

An appeal was taken to the Appellate Division of the Supreme Court of the State of New York held in and for the First Judicial Department by your appellants from each and every portion of the decree with certain exceptions not here material (Record on Appeal, pp. 4-5, fols. 12-14). Said Appellate Division of the Supreme Court by its order dated April 2, 1942, as resettled on April 16, 1942, unanimously affirmed said decree (Record on Appeal, p. 248, fol. 744).

Thereafter, the appellants appealed to the Court of Appeals of the State of New York from said order of said Appellate Division "in so far as it sustains the constitutionality of Section 17-c, subdivision 2, of the Personal Property Law of the State of New York" (Record on Appeal, p. 236, fol. 706). Thereafter, and on the 15th day



of January, 1943, the Court of Appeals handed down its opinion, two judges dissenting, sustaining in all respects the constitutionality of said statute and affirming said order of said Appellate Division, and by its order dated said day and entered on the 25th day of January, 1943, in the Surrogate's Court, New York County, said order of said Appellate Division was affirmed (remittitur annexed to Record on Appeal).

**8. Opinions of the State Courts Necessary to Ascertain the Grounds of the Decree of the Surrogate's Court, the Order of the Appellate Division and Judgment of the Court of Appeals.**

The following opinions which may be necessary to ascertain the grounds of the Decree of the Surrogate's Court, the order of the Appellate Division and judgment of the Court of Appeals are hereto annexed and marked as indicated:

A. The opinion of Surrogate Foley, dated March 8, 1941, reported in 175 N. Y. Misc. Rep., at p. 1044.

B. The opinion of the Court of Appeals of the State of New York by Judge Finch, with dissenting opinions of Judges Loughran and Lewis reported in 289 N. Y. Advance Reports, p. 423.

Said Appellate Division rendered no opinion in unanimously affirming the decree of the Surrogate's Court.

**9. Grounds Upon Which It Is Contended That the Federal Questions Involved Are Substantial.**

That the questions here involved are substantial is perhaps best indicated by the fact that, subsequent to the decision in the instant case by the Surrogate of the County of New York, the other Surrogate of said County, in *Matter of Wacht*, 32 N. Y. Supp. (2d) 871 (not officially reported) condemned the statute in question as invalid, and two of the

judges of the Court of Appeals of the State of New York wrote separate dissenting opinions in which they similarly expressed the view that the statute was unconstitutional.

Your appellants contend that prior to the enactment of Section 17-c of the Personal Property Law of the State of New York, the law of that State with respect to the distribution as between principal and income of rents and the proceeds of sale of real property, acquired by a trustee on the foreclosure of a mortgage, had been established by the courts of that State, and that the law with respect thereto was a law of property.

They further contend that said statute deprives them of their property without due process of law, in that it directs the trustee to pay to the life beneficiary of the trust established by the will of Henry C. West rents from parcels of real property resulting from mortgage investments, which, under the law as enacted by that statute constituted principal of the trust which was payable to the remaindermen of said trust who are represented by your appellants. In this connection, they point out that the trust involved herein was established prior to the enactment of the statute. The mortgages in question were acquired by the trustee prior to the enactment of the statute. The real property was acquired on foreclosure or by deed in lieu of foreclosure prior to the enactment of the statute, and some of the rents received from such parcels of real property affected by the provisions of the statute were received prior to its enactment.

Under the law as it had been established by the courts of New York prior to the enactment of Section 17-c of the Personal Property Law, property acquired in salvage of a mortgage investment held by a trustee was deemed to be held by the trustee upon a trust for the sale thereof. Expenses of the foreclosure and in discharging tax liens and other charges against the property, accrued to the date of

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foreclosure, were to be temporarily advanced by the principal of the trust in which such mortgage was held. Likewise, costs which might be incurred in the operation of the property after foreclosure were to be advanced from principal. All sums advanced out of the principal of the trust in which the mortgage was held in connection with such mortgage operation were regarded as in the nature of a first mortgage or charge against the property. Subject possibly to a discretionary power in the trustee to distribute as income some of net rents, such rents were to be applied first toward repaying principal advances. After such principal advances had been repaid, then net rents might be paid over by the trustee to the life beneficiary as income, provided the amount of such rents did not exceed the amount which might be found due to the life beneficiary upon the completion of the salvage operation. Upon the sale of the real property, the proceeds of sale were to be applied as follows:

1. Any principal advances which had not been repaid out of the principal were first to be discharged. The balance of the proceeds, plus any net rents from the property which had not been used to discharge principal advances, were to be equitably apportioned between the principal and income of the trust, in the ratio which the principal of the mortgage bore to the amount of the interest from the date of default, which would have been earned on the mortgage had it not been foreclosed. From the amount apportionable to income, there was deductible any net rents theretofore credited to income (*Meldon v. Derlin*, 31 App. Div. 146, 158, aff'd 167 N. Y. 573; *Matter of Chapal*, 269 N. Y. 464; *Matter of Otis*, 277 N. Y. 101, reargument denied 277 N. Y. 650). There was some indication in the reported cases to the effect that the trustee had some discretion to effect a distribution, as, for example, of some of the rents received from such a parcel of real property. However, it appears that if the trustee paid the life beneficiary more than the amount, which on completion

of the salvage operation was found to be apportionable to income, the trustee was liable therefor (*Matter of Brainerd*, 169 N. Y. Misc. 640).

The statute attempted to modify these rules. It provided that, if in any year the trustee receives net rents, it should pay therefrom to the life tenant up to three per centum of the principal amount of the mortgage. Such payments were required regardless of whether moneys advanced out of the principal of the trust to pay for the expenses of the foreclosure, arrearage of taxes, or other capital improvements had been repaid. The rule that the first duty of the trustee was to repay those principal advances out of any moneys received, whether by way of rents or sale of the real property, was abolished.

As construed by the New York courts, the statute requires that net rents received in any year should be so applied, although in all previous years the property may have been operated at a deficit, so that for the whole period from the date the property was acquired by the trustee to the end of the year, no net rents would have been received by the trustee. Nevertheless, the statute would require the trustee to treat net rents received in such a subsequent year as a separate unit, and disregard the losses incurred in earlier years.

Moreover, the statute provides that the payments made to the life beneficiary as directed by the statute shall be final, and shall not be subject to recoupment from the life tenant, and further, that the trustee shall not be liable for surcharge for having distributed rents to the life beneficiary, as directed by the statute.

The demand of the statute is inexorable and leaves no discretion on the part of the trustee. Although the property is subsequently sold for a sum which is not sufficient in amount to repay the principal advances to provide for the expenses of the salvage operation, nevertheless, under

the terms of the statute the life beneficiary is entitled to retain as income the rents received and which became distributable to the life beneficiary under the provisions of the statute.

Thus it will be seen that, in effect; the statute directs that moneys which, under the law as established prior to the enactment thereof, constituted part of the principal of the trust created by the will of Henry C. West, and which, upon the termination of the trust would be distributable to the remaindermen who are represented by your appellants, should be paid over and distributed as income to the life beneficiary of said trust. In other words, the principal of your appellants is, by the statute required to be paid to the life beneficiary, and your appellants are thus deprived of their property without due process of law and in violation of the rights guaranteed to them by the Fourteenth Amendment.

Moreover, due process of law requires that the equitable interests of the life beneficiaries and remaindermen in existing trusts shall be determined only by the courts. Enactments attempting to affect such existing rights are without the power of the Legislature and, it is submitted, invalid under the Fourteenth Amendment to the Constitution of the United States.

Dated April 3rd, 1943.

GERALD P. CULKIN,  
*Special Guardian for William J.  
 Demorest, Jr., Ann Demorest  
 and Carolyn Demorest.*

**APPENDIX A.**

Opinion of Surrogate James A. Foley of New York County.

In the Matter of the Estate of Henry C. West, deceased.

175 Misc. 1042.

"FOLEY, S. In this accounting proceeding the answers of certain of the parties and the report of the special guardian have raised numerous issues involving salvage operations of mortgaged properties acquired by a trustee by foreclosure or by deed in lieu of foreclosure. Such issues involve in part questions as to the effect of the decisions of the Court of Appeals in Matter of Chapal (269 N. Y. 464) and Matter of Otis (276 id. 101), and in part the effect of the recently enacted section 17-c of the Personal Property Law, which modified in certain phases the former rules in salvage operations. The briefs of the various attorneys have analyzed these questions with commendable thoroughness.

Under the terms of the testator's will, the residuary estate was devised and bequeathed in trust, 'to apply the net income from said estate to the use of my wife, Emma M. West, during the term of her natural life, or until she shall remarry.' Upon the death of the testator's widow, the estate was directed to be continued to be held in trust upon certain shares for the benefit of a nephew and a niece of the testator, with contingent remainders. The trust is still in effect.

At the date of his death the testator owned a number of entire guaranteed mortgages. Title to nine of the properties, upon which the mortgages were liens, was acquired by the executor either by foreclosure sale or by deed in lieu of foreclosure. By the decree of this court, dated August 10, 1936, upon an accounting by the executor, the properties so acquired were directed to be transferred by the executor to itself as trustee, as assets of the trust, to be held in separate account by the trustee. Questions as to the apportionment of the proceeds received upon the ultimate sale of the properties and the respective rights of principal and income beneficiaries in them were reserved for determination by decree in a subsequent accounting proceeding of the trustee.



The trustee has now accounted for the operation of each of these properties. The account discloses that as to seven of the properties the salvage operations are still unfinished. The operation of the other two properties is complete, since they were resold prior to the enactment of section 17-c of the Personal Property Law—one for cash and the other for part cash and part by the execution and delivery of a purchase-money mortgage. No distribution, however, has been made of the proceeds of sale of either of these properties.

The issues raised may be summarized as follows:

First. The constitutionality of subdivision 2 of section 17-c of the Personal Property Law (added by Laws of 1940, chap. 452, effective April 13, 1940) which modified, in certain respects, the prior rules in mortgage salvage operations.

Second. If constitutionality be sustained, the effect of the terms of that subdivision upon salvage operations falling within its scope.

Third. The determination of new questions not arising under section 17-c of the Personal Property Law and not decided specifically by the Court of Appeals in *Matter of Chapal* (supra) and *Matter of Otis* (supra) or by other authorities dealing with mortgage salvage operations.

First. In the consideration of the constitutionality of new section 17-c of the Personal Property Law, the prior decisions of the Court of Appeals, the existing situation in trusts, the reasons and conditions which led to its enactment and the terms of the section itself become important. The Chapal-Otis rules had, to a great extent, simplified the problem of the trustee, the lawyer and the courts of first instance, in dealing with particular situations developed before them. But complications still remained in salvage operations.

As the economic depression subsequent to 1929 deepened and the value of real properties melted, a waive of foreclosures resulted. Mortgages, which had been regarded in former years as attractive and desirable investments for trust funds, created after foreclosure or acquisition of title complicated and difficult questions with the imposition of

burdensome expense to persons interested in trust estates. The complications involved in the computation in a pending or completed salvage operation are emphasized in the pending proceeding where the mathematical analyses and the supporting schedules cover fifty-one closely typed pages of the account. The solution of these problems became the subject of study by members of the bar and particularly by those who were specialists in the law of trusts and estates. In liaison with the executive committee of the Surrogates' Association of our State, intensive investigation was made with the objective of simplification of the rules applying to mortgage salvage operations. Two solutions were immediately presented. The first involved a repeal of the Chapal-Otis rules in their entirety, with a recommendation to the Legislature to enact a statute which would treat the foreclosed or acquired real property as a capital asset in the same manner as ordinary real estate left by a testator. If the foreclosed real estate was thus treated as a capital asset, net income derived from the property would become immediately payable to the life tenant. Upon a sale of the realty, the proceeds would be treated as part of principal. Upon such sale, no allocation between life tenant and remainderman was required. Such was the form of the statutory relief passed by the Legislature of Connecticut. (Pub. Acts (1939), chap. 232.)\* The obstacle to the recommendation of the passage of such a sweeping statute, despite the common sense approach which motivated it, was the belief by some of the conferees that if it were applied to mortgage investments made before the effective date of the new statute, it might be subject to the hazards of a determination of unconstitutionality. The second alternative of those who drafted and recommended the passage of the statute by the Legislature was to divide the problem into two parts. The division provided, first, for the abolition of salvage operations as to future investments in mortgages and, second, with the major objective of assisting life tenants, for the modification, within constitutional limits, of the existing law as to investments in mortgages made prior to the effective date of the statutory amendment. That program was ultimately adopted and is embodied in new section 17-c of the Personal Property Law.

Its first subdivision abolished the Chapal-Otis rules as to testamentary trusts of persons dying after the effective date of the statute and as to inter vivos trusts thereafter established. It likewise was made to apply to mortgage investments made after such effective date in existing trusts, whether testamentary or inter vivos. As to such trusts and mortgaged real property the new subdivision stated that the 'real property shall be and become a principal asset in lieu of' the mortgage. The 'tenant or tenants for life or limited term shall be entitled to the net income from such acquired real property from the date of its acquisition.' The rules of procedure under the Chapal-Otis decisions were 'abolished'. Any allocation or apportionment between life tenant and remainderman was prohibited. In the pending proceeding no question has arisen as to the constitutionality of such first subdivision. Indeed no such question would be tenable since its provisions were wholly prospective in operation.

We now come to the consideration of the terms of the second subdivision of the section, the constitutionality of which is in dispute here. Two relatively simple modifications of the Chapal-Otis rules were made in this subdivision. Under those rules and particularly under the language of the opinion of Judge Loughran in *Matter of Otis* (supra), a discretionary power was given to a trustee during a mortgage salvage operation to disburse income to the life tenant, after advances made from principal as an incident to the acquisition of the property had been repaid. It was found, however, that trustees hesitated to make any payment to the life tenant or to exercise the judicial discretion given to them by *Matter of Otis*, because of the fear of a possible surcharge in the event of an overpayment to the life tenant. The life tenant in almost every instance was the primary object of the testator's bounty. The beneficiary intended to be most favored was thus deprived, by the trustee's inaction or hesitancy, of receiving income during the entire salvage period and large sums of money were accumulated and frozen. The injustice to the life tenant was aggravated by the fact that because of the lack of a ready market for the resale of the property, the salvage operation was unduly

extended for a long period of years. This situation is emphasized by the facts revealed in the present proceeding. Of the seven mortgages now involved in the salvage operations in which no resale has taken place, the longest period of operation has been six years and two months. The shortest period has been four years and ten months. Thus the average period of operation of all seven mortgages has been approximately five years. In the two completed operations the periods of salvage were two years and six months and two years and eight months. This unhappy situation has been corrected by the new legislation. Trustees are expressly authorized to pay promptly net income derived from the foreclosed or acquired property up to three per centum per annum upon the face amount of the mortgage. From the time of the passage of the new act, it has been the practical experience and observation of the surrogates that hundreds of thousands of dollars which had been theretofore accumulated, were paid out to life tenants upon the authority granted by the statute. Where the trustee had paid the yearly income up to the three per cent maximum to the life tenant, the statute made the payment final. It was specifically stated by the Legislature that such payment up to the maximum was 'not subject to recoupment from the life tenant or as a surcharge against the trustee or executor.' Moreover, under the new statutory rule, net income up to the maximum of three per cent became payable from the very beginning of the salvage operation, that is, from the date of acquisition by foreclosure or by deed in lieu of foreclosure.

The other amendment to the Chapal-Otis rules made by the second subdivision of the new section in the balancing of the equities, furnished protection to the remaindermen interested in the principal of the trust. Excess net income earned in any one year during the salvage operation above the three per cent maximum payable to the life tenant, was directed to be applied to advancements from principal for arrears of taxes and other liens which accrued prior to the foreclosure or acquisition in lieu of foreclosure and to the cost of capital improvements. Where any balance of unpaid principal advances remained due at the close of the

salvage operation, such balance was declared to be 'a primary lien upon the proceeds of sale and shall be paid first out of any cash so derived. If insufficient the balance shall be a primary lien upon any purchase money mortgage received upon the sale.'

The special guardian of the infant remaindermen has, perhaps, by way of formal objection with a view to a review of this decision by the appellate courts, raised the issue of unconstitutionality. By that procedure it is hoped by all those interested in this program of law reform, that the constitutionality of the new statute will be forever quieted. In essence, therefore, this proceeding is to be regarded as a test case. The special guardian contends that the new statute deprives his wards of property rights and that it is violative of the due process clause of the Fourteenth Amendment of the Federal Constitution and of the similar clause contained in our State Constitution.

His specific attack is based upon the retroactive provisions of the new second subdivision which apply to mortgage investments made previous to its enactment or to salvage operations initiated prior to such enactment. It provides: 'The terms and rules of procedure of this subdivision shall apply specifically (a) to the estates of persons dying before its enactment, and (b) to mortgages on real property held by a trustee under a deed of trust or other instrument executed before the date of its enactment, and (c) to real property acquired in lieu of foreclosure before or after the date of its enactment in trusts created or mortgage investments made prior thereto, and (d) to any pending proceeding or action for an accounting of the transactions of an executor or trustee.' It is claimed that the effect of that subdivision was to take away property from the remainderman in so far as the amounts paid to the life tenant up to the maximum of three per cent per annum might exceed the income allocable to him under the Chapal-Otis rules at the close of the mortgage salvage operations.

All of these contentions are overruled. The provisions of the new subdivision are merely remedial, procedural and administrative. The Legislature has done no more in



formulating a modification of existing rules than the courts themselves could do and have done within their constitutional powers. In a general sense the rules as to these salvage operations have been in a fluid state and have never been absolutely or finally fixed by the courts in their application to existing trusts or prior salvage operations. The strongest support for that conclusion is found in the opinion of Judge Loughran in *Matter of Otis* (supra). He there stated, 'Perhaps it should be added that a general rule for such situations cannot be attained at a bound, that no rule can be final for all cases and that any rule must in the end be shaped by considerations of business policy. Accordingly, we have here put aside inadequate legal analogies in the endeavor to express fair, convenient, practical guides that will be largely automatic in their application. Only the sure result of time will tell how far we have succeeded.' (*Matter of Otis*, supra, p. 115.) The 'sure result of time' had led the Legislature to make the changes of procedure upon the ground of necessity and advisability by the enactment of the new subdivision. The traditional tests of a statute are the old law, the mischief and the remedy. It is the duty of the courts so to construe the act as to suppress the mischief and advance the remedy. The legislative purpose was declared in the statute itself in subparagraph (d) of subdivision 2 of the section. It reads: 'The purpose of the enactment of this subdivision is declared to be the simplification of the rules of procedure in mortgage salvage operations and the elimination of present complications which would be to the disadvantage of the life tenant, who is usually the principal object of the testator's or settlor's bounty, by depriving him of a fixed right to the actual payment of any net income earned by the property. Such fixed right is granted in lieu of the discretion now given to the trustee to pay net income or any part thereof to the life tenant. The general rules of the apportionment of the proceeds of sale between life tenant and remainderman are retained subject to the express modifications made herein. Only equitable adjustments and balances as between the parties are intended to be effectuated by the provisions of this subdivision.'



The additional reasons which moved the Legislature to modify the existing rules under the Chapal-Otis decisions are stated in the explanatory note which was printed in the legislative bill. It is indicative of the intent of the Legislature. It reads in part: 'The Chapal-Otis rule authorizes the trustee to pay surplus net income in his discretion. Trustees have hesitated to pay such net income because in the case of overpayment to the life tenant, the trustee might be surcharged with that amount. The life tenant of the trust must wait in the majority of cases for a long period of time before he becomes entitled to the payment of any income, because of the present requirement that advances from principal for the expenses of foreclosure and for arrears of taxes and other liens must first be paid from the net income of the property. The amendment provides for the immediate payment of income to the life tenant beginning with the date of the acquisition of the property by the trustee by foreclosure or conveyance in lieu of foreclosure.'

Again, the nature of a salvage operation was described in *Matter of Otis* (supra), as a resort to fictions. 'Both capital account and income account, as described in the Chapal case, are fictions. \* \* \* If, then, the remaindermen are to participate in the apportionment on the feigned basis of unimpaired principal, the share of the life tenant should be computed on the same assumption. The invention of the 'original investment' is no more valid than the invention of 'unpaid interest' thereon. Indulgence in both fictions keeps the balance even between the respective parties in interest.' Under the 'historic fictions' of the English law and the modern fictions which exist under our own law, their ineptness have led to change and improvement by the courts which had to apply them. This very ineptness also constituted an invitation to Parliament in England, and to our own Congress and Legislatures, to alter the fictions, particularly in procedural matters, in order to correct injustice. Fictions, as stated by Professor Gray, were invented and altered 'in order that the wine of new law might be put into the bottles of old procedure.' (Gray, *The Nature and Sources of the Law*, p. 34.) The fiction was always capable of modification to meet the needs of modern justice.

Alterations of rules of procedure or administration made by the Legislature or by the courts, do not change substantive rights. Rules of procedure may, therefore, be modified, added to or repealed as the exigencies of the law and particular situations require. 'Nor has a person a vested interest in any rule of law entitling him to have the rule remain unaltered.' (*Preston Co. v. Funkhouser*, 261 N. Y. 140; *affd.*, sub nom. *Funkhouser v. J. B. Preston Co.*, 290 U. S. 163, citing *Truax v. Corrigan*, 257 id. 312, 348.)

It is claimed that the effect of subdivision 2 of section 17-c was to take away property from the remainderman, in so far as the amount ultimately payable to him on a sale of the real property might be less than the amount which would be payable to him under the rules laid down in *Matter of Chapal* (*supra*) and *Matter of Otis* (*supra*). The possibility that such a situation might result is infinitesimal. Two factors show the extreme improbability of the occurrence of such an event. The customary mortgage interest rate for several years past has been five per cent per annum. The maximum amount payable to the life tenant, under the new statute is three per cent. There is, therefore, a margin of safety of two per cent available in the average case in the final computation of allocation to income. Again, a property which would yield three per cent net per annum would, in all probability, produce a selling price sufficient to pay the life tenant, after final apportionment, a sum in excess of what had been paid within the statutory maximum during the period of salvage operation.

Many remedial rules of procedure or administration have created new rights not theretofore existing, which ultimately benefited one person as against another. The constitutionality of such legislation, even though it were retroactive in its application to existing actions or proceedings or to the estates of those dying before the statutory change was enacted, has been time and again sustained by the courts in the interest of uniformity and justice. As, for example, in *Preston Co. v. Funkhouser* (*supra*), our Court of Appeals and the United States Supreme Court upheld, as constitutional, a statute retroactive in scope providing that in any action for the enforcement of or based upon

breach of performance of a contract, interest shall be allowed upon the sum awarded, whether theretofore liquidated or unliquidated. In that case, the Court of Appeals, through Judge POUND, said: 'Every change in the remedies open to parties to a contract does not constitute an impairment of its obligation. Where the statute deals only with the remedy, the creation of a new and more adequate remedy does not impair the obligation of the contract. (*Sackheim v. Pigueron*, 215 N. Y. 62) \* \* \* It follows that section 480 is a remedial statute to be construed, according to its literal meaning, to apply to all actions brought after it went into effect, irrespective of the time when the cause of action arose. It changes an existing right of action rather than creates a new right.' The court also pointed out that 'the mere fact that the statute is retroactive does not bring it in conflict with the Federal Constitution.'

It has always been the recognized function of the courts to promulgate rules of procedure and administration for the guidance of fiduciaries in their conduct of trust estates. Such rules have also found expression from time to time by enactment in the various statutes of our State. Examples of remedial statutes modifying or establishing rules of procedure in the administration of existing trusts, where their reasonableness and constitutionality have been sustained, are many. In *Matter of Robertson v. de Brulatour* (188 N. Y. 301), after the death of the testator, the Legislature established a new and different rule covering the compensation of trustees: An increased measure of compensation was provided. The trustees were held to be entitled to their benefit and commissions were allowed to them under the statute in effect at the date of the accounting. In *Matter of Barker* (230 N. Y. 364), commissions for receiving assets were allowed to the estates of deceased executors pursuant to a statute in effect at the date of the accounting but which was not enacted until subsequent to the death of the executors, and necessarily of the testator. In referring to the retroactive effect of the statute, the court there said: 'The general rule is that the fees of an executor are to be fixed by the rules and law which prevail at the time when they are settled. (*Robertson v. de Brula-*

tour, 188 N. Y. 301, 316, 317; *Whitehead v. Draper*, 132 App. Div. 799.) In the last case this principle was applied in the opinion written by Justice MC LAUGHLIN in a case where the statute invoked in aid of an executor's commissions was not passed until after his death. This is quite akin to the rule that remedies will be applied in accordance with the law which prevails at the time when relief is sought rather than at the time when the injury arose (*Matter of Berkowitz v. Arbib & Houlberg, Inc.*, 230 N. Y. 261.)

Other instances of remedial statutes may be found in (1) those modifying, after the death of the decedent, the classes of legal securities in which trustees are authorized to invest (*City Bank Farmers Trust Co. v. Egans*, 255 App. Div. 135; *Matter of Hamersley*, 152 Misc. 903; (2) the provisions of the Surrogate's Court Act (SS 225 and 226), providing that an administrator with the will annexed or a successor trustee may exercise powers granted to an executor or trustee to mortgage, lease or sell real property (*Hollenbach v. Born*, 238 N. Y. 34); (3) the sections of the Real Property Law authorizing the sale of real property where the interests are both possessory and future (*Matter of Mersereau*, 233 N. Y. 540; *Matter of Gaffers*, 254 App. Div. 448) and (4) the statute granting a creditor of an income beneficiary of a trust the right to require that ten per cent of the income be applied in satisfaction of his claim or debt. (*Brearley School v. Ward*, 201 N. Y. 358.) The constitutionality of each of these legislative enactments was sustained.

In *Reiner v. Fidelity Union Trust Co.* (126 N. J. Eq. 78; 8 A (2d) 175; revd. on other grounds, 127 N. J. Eq. 377; 13 A. (2d) 291) a statute giving the Court of Chancery of the State of New Jersey power to authorize or direct trustees to invest in securities other than those listed by the statutes as legal for trust investments was upheld as constitutional. The court there said: 'The statute does not purport to authorize the court to change substantive rights. It has reference merely to matters of administration.'

The extent to which courts have gone to sustain rules of procedure and administration is evidenced by the decision of the United States Supreme Court in *Kuehner v. Irving*.

Trust Co. (299 U. S. 445). There, the constitutionality of clause (10) of subsection (b) of section 77B of the Bankruptcy Act (U. S. Code, tit. 11, S. 207), which limited the claim of a landlord for indemnity under a covenant in a lease in a corporate reorganization to an amount not to exceed three years' rent, was considered. Prior to the passage of this provision of the Bankruptcy Act, such claim was not provable or dischargeable in a bankruptcy proceeding. Under the new statute, the landlord's claim was allowed to the extent of three years' rent only. The rental value for the balance of the term of the lease under the rent fixed by the lease greatly exceeded the three years' rent allowed. It was asserted that this limitation offended the due process clause of the Fifth Amendment of the Constitution of the United States. The validity and constitutionality of the statute were sustained as giving a new and more certain remedy for a limited amount in lieu of an old remedy, insufficient and uncertain in its result. The statute was held to be fair and reasonable and to create uniformity of treatment of a peculiar class of claims, difficult of liquidation. It was held not to be the taking of the landlord's property without due process of law.

As applied to existing trusts, the above authorities clearly support the validity of the remedial legislation enacted in subdivision 2 of section 17-c of the Personal Property Law.

The rules under the subdivision are just, fair and reasonable. Only equitable adjustments and balances as between principal and income beneficiaries were declared to be effectuated by its provisions. It was within the province and power of the Legislature to enact them. The objection of the special guardian, therefore, addressed to the constitutionality of the statute is overruled.

Second. Such determination of constitutionality requires the surrogate to pass upon the various questions raised as to the effect of the terms of the new subdivision upon mortgage-salvage operations within its scope. These questions are stated and discussed seriatim as follows:

(a) Does the section apply to the salvage operation of property acquired by a trustee which was sold before April 13, 1940, the effective date of the statute, where the distri-



bution has not been closed by a decree upon a judicial settlement of the account or by a written or other valid agreement between the parties for a voluntary distribution?

The surrogate holds that where the salvage operation has been completed before the effective date of the new section, its terms do not in any way alter or change the rights of the parties. Once the salvage operation is finished before that date, there remains nothing to be done except to make the computation of apportionment and to distribute under the Chapal-Otis rules. The terms of the statute apply only to uncompleted salvage operations at the date of its enactment or to operations initiated subsequent to such date.

(b) As to operations uncompleted at the effective date of the new section, shall payments to the life beneficiary of net income, when earned, up to a maximum of three per cent per annum upon the face amount of the mortgage be computed upon an annual basis, or shall the entire period of operation, if extending over a period of more than one year, be considered in such computation?

The answer is obvious. The statute clearly contemplates that the net income payments shall be based upon the annual income of the property and not upon the income for the entire period of the unfinished operation. It provides (Pers. Prop. Law S. 17-c, subd. 2, Par. (a): 'Net income during the salvage operation up to three per centum per annum upon the principal amount of the mortgage shall be paid to the life tenant . . . (Italics mine.) Annual rents and annual balancings of the account must thus be employed and the result of the *of the* operation of each parcel of property for each year must be treated as a separate entity in the computation and payment of the maximum net income permitted by the statute to be paid to the life beneficiary. It is an elementary rule in the administration of trusts that the computation of net income payable to a life tenant is based upon the yearly period, unless the terms of the will fix some other period. Any other policy would permit serious prejudice on the part of the trustee as against the life tenant by the withholding of accumulated income.

If, therefore, under this method of computation there are deficits of net income in lean years, they may not be made



up from surplus net income in productive years. Income earned in any one year in excess of the three per cent maximum payable to the life beneficiary and after repayment of principal advances, must be retained. Under the new section, principal advances 'shall be repaid out of excess net income above such three per centum per annum. When principal advances have been satisfied, any excess income shall be impounded \* \* \* to await sale and apportionment'. If the payments of income to the life beneficiary were not based upon annual rents, and the deficiency of net income payments in lean years could be satisfied from excess income in good years, the provision of the statute that such excess income shall be impounded would be nullified.

(c) In the computation of the net income payable to the life beneficiary, shall the fiscal year beginning with the date of the acquisition of the real property be used or shall the calendar year be employed?

I hold that the anniversary date of the computations of the annual payments to the life beneficiary is the date of the acquisition of the real property and annual rents shall be based upon that date. The period of salvage begins from the date of acquisition of the mortgaged property. (Matter of Otis; supra). The net income payable to the life beneficiary must be computed upon rents received during the fiscal year beginning with that date. It is not based upon rents received during the calendar year. The explanatory note printed in the legislative bill states: 'The amendment provides for the immediate payment of income to the life tenant beginning with the date of the acquisition of the property by the trustee by foreclosure or conveyance in lieu of foreclosure.' The statute provides that net income shall be paid during the salvage operation. The annual accounts and the computation of the amount due the life tenant at the statutory rate up to three per cent per annum must be based upon the recurring periods of one year from the anniversary dates of acquisition.

(d) Where net rents up to a maximum of three per cent per annum have been paid to a life beneficiary during the period of salvage, has the new section changed the method of apportionment to be made after sale, as laid down by the

rules in Matter of Chapal (supra), and Matter of Otis (supra)? In other words, has the formula for the allocation, as between income and principal, been changed by the terms of the new section? The surrogate holds that no change was intended by the Legislature.

The new section merely makes mandatory the payments of three per cent of net income each year to a life beneficiary when earned. It does not, however, change the formula for ultimate apportionment of the net proceeds of the salvage operation between life beneficiary and remainderman. Again the new subdivision provides: 'The existing rules of procedure applying to salvage operations respecting existing mortgage investments are continued except as modified by the subparagraphs hereinafter set forth.' As stated in Matter of Chapal (supra): 'In such an investment situation what is involved is the salvage of a security. The security . . . is a security not for principal alone but for income as well.' Paragraph (a) of subdivision 2, with a view to protecting the interests of both life tenant and remainderman in such securities and to impartial and fair apportionment, provides as follows: 'The amount of all such payments shall be taken into account, however, in the apportionment of the proceeds of sale and shall be charged against the share of the life tenant.' All net income, therefore, including such as had been paid to the life beneficiary during the salvage period, must be added to the proceeds of sale of the property as the total salvage fund. Out of such total there shall first be deducted the amount required for repayment of principal advancements. The balance then remaining shall be apportioned according to the Chapal-Otis formula between income and principal. After the share due the life beneficiary has been computed upon such apportionment, there shall first be credited upon such share the net amount of rents paid to the life beneficiary during the salvage operation as an advancement to income. The amount so paid to the life beneficiary must be 'charged against the share of the life tenant' under the new section. The amount apportioned to income, less the income advanced to the life tenant, shall be the balance which the life tenant shall then be paid out of the proceeds of the salvage operation. This method of determining the ultimate shares allocable to income and principal unquestion-

ably, in my opinion, accords with proper accounting practice. (Matter of Chapal, *supra*; Matter of Otis, *supra*; Matter of Brainerd, (Wingate, S.) 169 Misc. 640, 644.)

Third. The questions presented for determination in this group do not arise out of the provisions of the new section. They involve problems that have not directly been passed upon by the Chapal-Otis cases or by other authorities.

(a) Where a trustee has taken over property under foreclosure or by deed in lieu of foreclosure and finds it in such condition as to require rehabilitation, are the expenses incurred to put the property in a tenantable condition exclusively capital charges to be treated as advancements from principal, or are they income charges?

The surrogate holds that where at the time of the acquisition of the real property, the premises were not in rentable condition the cost of putting them into such condition is payable out of principal. The cost of thereafter maintaining the premises in repair and in tenantable condition is payable out of income. Under the new paragraph (a) of subdivision 2, the 'cost of all capital improvements' is made a principal charge.

As applied to ordinary trust property where no salvage operation is in effect, the rule seems generally to be well settled that where real property is originally received by the trustee in an untenable condition, the cost of rehabilitation is chargeable against principal. (Restatement of the Law of Trusts, comment i, § 233; *Stevens v. Melcher*, 152 N. Y. 551; *Matter of Deckelmann*, 84 Hun. 476; *Matter of Suydam*, 138 Misc. 873; *Smith v. Keteltas*, 62 App. Div. 174; *Matter of Heroy*, 102 Misc. 305.)

In the Restatement of the Law of Trusts the following appears: 'The cost of putting into tenantable repair premises which were not in such repair when received by the trustee, whether originally acquired by the trustee as part of the trust property at the time of the creation of the trust or subsequently acquired by him, is payable out of principal; but the cost of thereafter keeping the premises in repair is payable out of income.' The application of this rule to salvage operations would appear to be for the best interests of both life beneficiary and remainderman. Whenever necessary repairs or structural changes are made to

put real property in a rentable condition, there inures a benefit to both principal and income beneficiaries. The expenses of rehabilitation, therefore, which are incurred upon the acquisition of the property should be treated as advancements from principal and charged to principal. On the other hand, all expenditures for current repairs and those which are incidental to the management of the property, during the period of the salvage operation, should be charged to income under the general rule laid down in *Matter of Albertson* (113 N. Y. 434). The surrogate sustains the objections of the special guardian to the payment from principal of sums for the current repair and maintenance of the premises, other than the expenses of putting them into tenantable condition at the date of the acquisition of the property. If the parties are able to agree as to the items properly chargeable to income under this determination, a stipulation may be filed within ten days of this decision. If agreement is not reached, the matter will be set down for a further hearing upon this issue.

(b) The further question has been raised as to what is the method of apportioning dividends which may be received in payment, partially or in full, of claims arising out of the guaranty against loss resulting from a defaulted mortgage by an insolvent mortgage guaranty company. Certain sums have been received by the trustee in this estate on claims allowed by the Superintendent of Insurance, as liquidator of the Bond and Mortgage Guarantee Company. All of the properties involved were acquired by foreclosure or by deed in lieu of foreclosure prior to December 31, 1937. The order of liquidation was made and the rights of the parties under the Insurance Law are to be determined as of that date.

The obligation of the Bond and Mortgage Guarantee Company constituted a guaranty as to both interest and principal. The trustee filed proofs of claim with the Superintendent of Insurance. These claims covered the deficit of interest up to December 31, 1937, and the alleged liabilities of the guarantor for restitution of principal losses. In each case the default in interest was allowed by the Superintendent in full. The claims for principal charges were substantially reduced by him.

The surrogate holds that liquidating dividends when received must be treated as part of the general funds developed from the salvage operation. In this sense they are like rents received and the proceeds of sale of the acquired real property. The allocation made by the Superintendent of Insurance as between the guaranty of losses incurred in income and the guaranty of losses incurred in principal is to be treated as tentative only. In addition, all of the parties here conceded that because of the very large liabilities of the guaranty company, the dividends will be relatively small in amount. Moreover, the application of these liquidating dividends should be made as simple as possible.

With this objective in mind the surrogate holds that as to dividends received for income losses from the Superintendent of Insurance, such amounts should be added to the income (derived as rents) during the specific year of the actual receipt of the liquidating dividends. This addition to such rents may still leave a deficit in operation with no net rents available for the fiscal year. On the other hand, the addition may wipe out a deficit and produce a net income for such year. In the latter case the moneys become payable within the three per cent maximum to the life tenant. If there be any surplus above the three per cent maximum caused by the addition of these dividends, such surplus shall, under the rule of section 17-c, be applied on account of advances to principal, or if such advances have been satisfied, they shall be retained as part of the general funds of the salvage operation to await sale and final apportionment.

Any dividends received from the Superintendent of Insurance as tentative payments upon principal account shall likewise be retained as part of the general proceeds of the salvage operation to await final sale and apportionment, unless necessary to discharge unpaid balance of principal advancements.

Any dividends which may be received by the trustee on its claim under the guaranty of a mortgage subsequent to the completed salvage of such mortgage, should likewise be apportioned between principal and income in the same ratio



as has been applied to the proceeds of sale. They are additional proceeds of the salvage operation.

(c) Where the mortgage was originally guaranteed as to payment of interest and principal by a mortgage guaranty corporation and the guaranty has been canceled by the trustee, because of the insolvency of the corporation, shall the share of the life beneficiary be computed upon the rate fixed in the mortgage or at the rate agreed to be paid by the guaranteeing corporation? In other words, assume an original mortgage was made with six per cent interest. The corporation has reserved to itself, as the usual charge for the guaranty, one-half of one per cent per annum. The purchaser of the mortgage from the corporation became originally entitled to five and one-half per cent. Where the agency of the guarantor has been canceled, is the share of the life beneficiary to be computed for the duration of the period of salvage at six per cent per annum, the rate set forth in the instrument or at five and one-half per cent?

I hold that the rate of interest fixed in the mortgage taken over by the trustee from the guaranty company is the rate upon which the life beneficiary's interest must be computed. The Court of Appeals in *Matter of Otis* (supra) declared the rate of interest as fixed in the mortgage to be the rate to be used as a basis upon which allocation to income was to be made. It said: 'We prefer to adhere to our ruling in *Meldon v. Devlin* (167 N. Y. 573, affg. 31 App. Div. 146) that interest should be computed at the mortgage rate for the whole period.' Although the Court of Appeals in that case did not have before it the exact question here involved, its preference to the adoption of the rule which would fix the mortgage rate upon the cancellation of a guaranty, would appear to be clearly indicated. In view of the determination in *Matter of Otis* (supra), it is immaterial that only a yield of five and one-half per cent was guaranteed by the guaranty corporation.

Where, however, prior to acquisition by foreclosure or by deed in lieu of foreclosure, the trustee and the owner of the property have by agreement fixed a rate of interest below the rate prescribed in the mortgage instrument itself,



the reduced rate shall be used and not the mortgage rate. Such agreement for reduction of interest, if validly made, is binding upon the parties.

In the present proceeding, the trustee, by letter dated October 22, 1934, agreed to reduce the interest rate in the mortgage on one parcel of real property, 240 Floyd Street, Brooklyn, N. Y., from six per cent to four per cent. The interest of the life tenant in the salvage operation must, therefore, be computed at the latter rate from the date of such reduction to the date of sale.

(d) Further questions have been presented as follows:

Where there has been a resale of the foreclosed property and a purchase-money mortgage has been taken back, shall amortization payments under the new mortgage received by the trustee be applied primarily to the discharge of unpaid principal advances for the prior salvage operation, if any are still due? Where principal advances have been entirely repaid, shall amortization payments on the purchase-money mortgage be allocated between life tenant and remainderman as fixed upon apportionment of the proceeds of sale, pursuant to the applicable rules, upon the completion of the prior salvage operation?

The answer to each of these two questions must be in the affirmative. Since unpaid principal advances are a prior lien upon the proceeds of sale of the salvaged property (Matter of Chapal, supra; Matter of Otis, supra; Pers. Prop. Law, Sec. 17-c), principal has a prior interest in or lien upon the purchase-money mortgage taken back by the trustee upon the sale. In those circumstances, amortization payments made by the new mortgagor should be credited entirely to principal on account of such prior lien. When the principal advances have been entirely repaid, the amounts received for amortization should be apportioned between principal and income in accordance with the respective shares of each, previously computed and apportioned under the Chapal-Otis rule. The interest received by the trustee on the purchase-money mortgage I hold is payable to the life beneficiary. A similar conclusion was reached in Matter of Martin (165 Misc. 597).

(e) One further question requires disposition. It is claimed by the income beneficiary that she should be allowed interest at the prevailing rate upon the rents withheld from her by the trustee, which were distributable under section 17-c, from the date of their receipt by the trustee until their payment. The claim is disallowed. The surrogate holds she is entitled to no interest on such rents under the circumstances of this proceeding. In a case where the trustee arbitrarily refuses to pay, interest might be awarded against him for his recalcitrancy and by way of compensation for the detriment suffered by the life tenant.

The objections filed to the account herein are disposed of as follows:

Objections I, II, III, IV, V and VII filed by the special guardian are overruled. Objection VI, relating to the charging of expenditures for repairs, has been the subject of instructions and possible further hearing in the prior portion of this decision.

Objections 5 and 9 of the life beneficiary are overruled. The remaining objections filed by her are sustained to the extent of directing the necessary readjustments to be made in the account to comply with the conclusions of the surrogate contained in this decision.

Submit decree on notice settling the account in accordance with this decision and with the prior decision construing the will (175 Misc. 1042) made in this proceeding."

## **APPENDIX B.**

### **Opinion of Court of Appeals, 289 N. Y. 423, in Matter of West.**

In the Matter of the Estate of HENRY C. WEST, Deceased.  
WILLIAM J. DEMOREST, JR., et al., Appellants. CITY BANK  
FARMERS TRUST COMPANY, as Trustee, et al., Respondents.

Appeal by William J. Demorest, Jr., Ann Demorest and Carolyn Demorest, infants, and their special guardian, from an order of the Appellate Division of the Supreme Court in the first judicial department, entered April 16, 1942, which unanimously affirmed, so far as appealed from, a

decree of the New York County Surrogate's Court (Foley, J.) settling the accounts of City Bank Farmers Trust Company, as trustee under the will of Henry C. West, deceased, and construing the will of the testator. (See 175 Misc. 1042, 1044.) The appeal is from such order of the Appellate Division in so far as it sustains the constitutionality of subdivision 2 of section 17-c of the Personal Property Law (Cons. Laws, ch. 41).

Appeal by Emma M. West, by permission, from so much of such order of the Appellate Division as unanimously affirmed portions of the decree contained in articles 6, 7, 21, 22 and 26 thereof.

FINCH, J. The question presented for decision is the constitutionality and construction of the provisions of subdivision 2 of section 17-c of the Personal Property Law (L. 1940, ch. 452, effective April 13, 1940; Cons. Laws, ch. 41) in so far as the same modify retroactively the rules relating to mortgage salvage operations.

The new statutory rules allot to the life tenant out of the net income earned from the operation of real estate in salvage, an annual amount up to three per cent of the face value of the mortgage investment. Such right is granted in lieu of the discretion vested in the trustee under the heretofore existing rules of trust administration to pay net income or any portion thereof to the life tenant, a discretion which has not been exercised generally by trustees through fear of possible surcharge. Such payment of net income is made payable from the beginning of the salvage operation and is declared to be final and not subject to recoupment, either from the life tenant, or from the trustee or executor by way of surcharge. With the exception of the aforesaid modification, the previously existing rules governing salvage operations are continued except that annual net income in excess of the maximum sum payable to the life beneficiary, is directed to be held and further equitable adjustments upon the apportionment are also provided for, in order to insure to the remainderman that any unpaid advances from principal must be first repaid upon the final liquidation of the investment.

The validity of this statute has been put in issue upon this proceeding for an intermediate accounting by the trustee under the will of Henry C. West. By the terms of the testator's will, his residuary estate was devised to a trustee to apply the net income therefrom to the use of his wife during her life or until her remarriage. Upon the termination of the life estate, the trust was directed to be divided and continued upon certain shares for the benefit of a nephew and niece of the testator, with remainders over.

At the time of his death in 1934, the testator's residuary estate included, among various other assets, certain wholly owned guaranteed mortgages. Nine of these mortgages went into default after the death of the testator, and the estate acquired title to the real properties either by foreclosure or by deed in lieu of foreclosure prior to April 13, 1940; two of the properties were sold before that date, the income and proceeds therefrom, however, being retained in the hands of the trustee.

In the present proceeding the special guardian for the infant remaindermen contends, first, that the entire subdivision 2 of section 17-c is unconstitutional because it is expressly made retroactive in operation, and that, second, if constitutional, it does not apply, as a matter of construction, to the proceeds of the two properties which were sold before the statute became effective. The learned Surrogate sustained the constitutionality of the statute, but held as a matter of construction that it applied only to salvage operations uncompleted at the date of its enactment and hence was inapplicable to the two properties sold before it became effective. Upon appeal, the Appellate Division unanimously affirmed.

When a mortgage in default is foreclosed and title to the property is acquired by the trustee, the original mortgage investment is at an end and a salvage operation is initiated. (*Matter of Otis*, 276 N. Y. 101, 111, 112.) The real property thus acquired is substituted for the mortgage in the hands of the trustee and takes on the character of personality. (*Lockman v. Reilly*, 95 N. Y. 64, 71.) The trustee holds this real property so acquired and must administer it as an asset of the trust estate for the benefit of the life tenant and

the remaindermen. Like the mortgage, it is "security not for principal alone but for income as well." (*Matter of Chapal*, 269 N. Y. 464, 472.) With respect to the mortgages which the testator owned at the time of his death and with respect to any real property which might be acquired by the trustee following default in any of these mortgages, the testator as creator of the trust gave no express directions except the general direction of what is commonly understood by the use of the words "income" and "principal." After the initiation of the salvage operation, as before, both the life tenant and the remaindermen could compel the trustee to administer the trust and to apportion to each his just share of the income and principal, but not that of any particular asset of the trust. (*Lockman v. Reilly*, 95 N. Y. 64, 71; *Bennett v. Garlock*, 79 N. Y. 302, 320.) Although the rule requiring apportionment as between income and principal, of the proceeds of such sale has been long established (*Meldon v. Devlin*, 31 App. Div. 146; *affd.*, 167 N. Y. 573), the rules relating specifically to mortgage salvage operations were speeded in the process of formulation by the courts with the coming of the economic depression of the 1930's. In *Matter of Chapal* (269 N. Y. 464) this court said: "We have another problem—that of the liquidation of real estate acquired of necessity because of default on a mortgage investment." Concerning these rules thus worked out to meet the emergency resulting from widespread foreclosures, in *Matter of Otis, supra*, at page 112, we said: "Both capital account and income account, as described in the *Chapal* case, are fictions \* \* \*. If, then, the remaindermen are to participate in the apportionment on the feigned basis of unimpaired principal, the share of the life tenant should be computed on the same assumption. The invention of the 'original investment' is no more valid than the invention of 'unpaid interest' thereon. Indulgence in both fictions keeps the balance even between the respective parties in interest."

Moreover, we expressly said in the *Otis* case that the rules laid down were tentative only and not intended to be final. At page 115 it was said: "Perhaps it should be added that a general rule for such situations cannot be attained at



a bound, that no rule can be final for all cases and that any rule must in the end be shaped by considerations of business policy. Accordingly, we have here put aside inadequate legal analogies in the endeavor to express fair, convenient, practical guides that will be largely automatic in their application. Only the sure result of time will tell how far we have succeeded." It was also carefully pointed out that no hard and fast rule was laid down to guide the trustee in the disposition of net income earned during the salvage operation, but the disbursement of net income to the life beneficiary was left to the discretion of the trustee. In the *Otis* case we said at page 115: "• • • the trustee may distribute such surplus income in its discretion. (269 N. Y. at p. 470.) This discretion, moreover, should be exercised with appropriate regard for the fact that unless a life tenant gets cash he does not get anything in the here and now."

The Legislature has found, however, that trustees through fear of surcharge have accumulated surplus with the result that undue hardship has been visited upon life beneficiaries. Taking heed of this hardship at the request of the executive committee of the Surrogate's Association of the State of New York, the Legislature has declared its purposes in the statute itself. In part it reads: "The purpose of the enactment of this subdivision is declared to be the simplification of the rules of procedure in mortgage salvage operations and the elimination of present complications which work to the disadvantage of the life tenant • • • by depriving him of a fixed right to the actual payment of any net income earned by the property. Such fixed right is granted in lieu of the discretion now given to the trustee to pay net income or any part thereof to the life tenant. • • • Only equitable adjustments and balances as between the parties are intended to be effectuated by the provisions of this subdivision." Thus the Legislature has substituted in place of the discretion in the trustee permitting disbursement of surplus income, another more definite rule requiring some, albeit modest, payment of surplus income to the life beneficiaries. At the same time the Legislature has provided that additional income over and above the modest rate of payment shall be held until final adjustment, thus providing



for equitable adjustments and balances as between life beneficiaries and remaindermen upon final liquidation, and safeguarding, so far as reasonably possible, the rights of all interested parties. The statute provides: "Any payment of net income heretofore or hereafter made to the life tenant up to such three per centum per annum shall be final and shall not be subject to recoupment from the life tenant or as a surcharge against the trustee or executor. The amount of all such payments shall be taken into account, however, in the apportionment of the proceeds of sale and shall be charged against the share of the life tenant.

In thus formulating a rule that is final against recoupment for distribution of income received in excess of carrying charges, it does not appear that the Legislature has done more than direct a trustee to do what under the decisions of this court he has discretionary power to do. (*Matter of Otis, supra.*) Before the enactment of this statute, the life tenant could not have demanded as of right the payment to him during liquidation of more of the surplus income than he will receive under the statute. Neither does it appear that the remaindermen could properly have insisted that the trustee should be surcharged if in the exercise of his discretion he had paid to the life tenant the amount which the statute now directs. A statutory rule of administration which requires the trustee to apportion income in accordance with a fixed standard which in the exercise of administrative discretion the trustee would even without the statute have power to adopt does not, in our opinion, constitute a taking of property. The principle is applicable that "The mere fact that the statute is retroactive does not bring it in conflict with the Federal Constitution. . . . Nor has a person a vested interest in any rule of law entitling him to have the rule remain unaltered." (*Preston Co. v. Funkhouser*, 261 N. Y. 140; 144; *Munn v. Illinois*, 94 U. S. 113.)

As already noted, the rules of administration heretofore set forth were tentatively stated and expressly recognized as subject to change. Before a judicial declaration, thus tentatively stated, becomes a rule of property, it must have become permanently fixed and long continued. (*United*

*States v. Standard Oil*, 20 Fed. Supp. 427, 458; affd., 107 F. [2d] 402, cert. den. 309 U. S. 673.) In that case the court said: "However, before setting up a judicial declaration as a rule of property, we should require, at least, that it be fixed, long-continued, and relied upon by persons acquiring property, so that its repudiation would amount to a denial of due process." Nor can the statute in the case at bar be said to be arbitrary or capricious, but on the contrary, it is fair and reasonable and protects the interest of both income beneficiaries and remaindermen. As was said in *Thompson v. Siratt* (95 F. [2d] 214, 217): "To hold that subsection (n) is repugnant to the Fifth Amendment requires a finding that its provisions are arbitrary and unreasonable."

We have, therefore, in the case at bar, no taking of property, no contract right involved and no impairment of due process. This statute, therefore, cannot be held to be unconstitutional. (*Robertson v. deBrulatour*, 188 N. Y. 301; *Brearley School, Ltd. v. Ward*, 201 N. Y. 358.)

The sole remaining question is whether or not the statute is applicable in cases where the liquidation was complete before the date when the statute became effective, the income and proceeds of property being still undistributed in the hands of the trustee. We concur in the construction placed upon the statute by the learned Surrogate, namely, that its scope is limited to cases where liquidation of real property acquired is incomplete. This is in accord with the language of the statute which provides that net income "during the salvage operation" shall be paid to the life tenant. Even in a "pending proceeding" or "action for an accounting," the language of the statute confines its application to cases where liquidation is incomplete and where "during the salvage operation" a trustee has acted in accordance with the discretion at that time vested in him. The apportionment of the proceeds of the property, both income and principal, where liquidation was completed before the statute became effective must be determined in accordance with the rules heretofore formulated by the court.

The order should be affirmed, with costs to the respondent trustee and one bill of costs to the infant-appellants, William

J. Demorest, Jr., Ann Demorest and Charles Demorest, payable out of the fund.

LEWIS, J. (dissenting). The infant-appellants, by their special guardian, challenge the constitutionality of section 17-c, subdivision 2, of the Personal Property Law (Cons. Laws, ch. 41). The problem relates to the apportionment, between an income beneficiary and remaindermen, of income realized by a trustee from operations undertaken to salvage defaulted mortgages held by it as fiduciary. In this instance the mortgages in default were nine in number. The title to each mortgaged property came into the trustee either by foreclosure or by deed in lieu of foreclosure prior to April 13, 1940. Two of the properties were sold prior to that date, the avails of the sale being retained by the trustee.

The date last mentioned is important to our inquiry because it fixes the time when there became effective chapter 452 of the Laws of 1940 which added section 17-c to the Personal Property Law. It is the effect upon the rights of a life tenant and remaindermen of the retroactive provisions of subdivision 2 of that statute which has prompted the present challenge to its constitutionality.

Section 17-c of the Personal Property Law (added by L. 1940, ch. 452, effective April 13, 1940) provides rules for the administration of that portion of a trust fund in which is a real estate mortgage, held for the benefit of one or more tenants for life or a limited term with remainder over, where title to the mortgaged property has been acquired by the trustee by foreclosure or by conveyance in lieu of foreclosure. We are not here concerned with subdivision 1 of section 17-c which applies only to estates of persons dying, or trusts created, *after* its enactment and to mortgage investments made thereafter by a trustee of an existing trust. The challenge is to the constitutionality of subdivision 2 of section 17-c, the terms and rules of which "apply specifically (a) to the estates of persons dying *before* its enactment and (b) to mortgages on real property held by a trustee under a deed of trust or other instrument executed *before* the date of its enactment and (c) to real property acquired by foreclosure of mortgage or real property acquired in lieu of foreclosure *before* or after the date of its enactment in

trusts created or mortgage investments made prior thereto  
 • • •” (Emphasis supplied.) In particular our inquiry goes to that portion of section 17-c to be found in subdivision 2(a) which in general provides that, regardless of advances made from the principal of a trust for the expense of a foreclosure, or of a conveyance of mortgaged property in lieu of foreclosure, and regardless of the cost of all capital improvements, payments—not subject to recoupment—shall be made to the life tenant from the net income during the salvage operation up to three per cent per annum computed upon the principal amount of the mortgage.

Clearly subdivision 2 of section 17-c is retroactive. By its terms it presumes to affect acts which occurred, and rights which accrued, prior to April 13, 1940—the effective date of the statute. Among acts thus affected was the execution on December 14, 1928, of the testamentary trust here involved; among rights thus affected are those of the life tenant and the remaindermen in the proceeds from transactions undertaken by the trustee as a means of salvaging mortgages which were a part of that trust—mortgages which, as we have said, were “security not for principal alone but for income as well.” (*Matter of Chapel*, 269 N. Y. 464, 472.)

In the case last cited this court ruled that, upon a sale had in the course of a similar salvage operation (p. 472)—  
 “• • • the proceeds should be used first to pay the expenses of the sale and the foreclosure costs and next to reimburse the capital account for any advances of capital for carrying charges not theretofore reimbursed out of income from the property. Then the balance is to be apportioned between principal and income in the proportion fixed by the respective amounts thereof represented by the net sale proceeds. In the capital account will be the original mortgage investment. In the income account will be unpaid interest accrued to the date of sale upon the original capital.” (And see *Matter of Otis*, 276 N. Y. 101, 111; *Matter of McManus*, 282 N. Y. 420, 425.)

When the properties here involved came into the hands of the trustee, the rule of apportionment last quoted above was not a matter of grace, as the majority opinion herein

seems to hold. It was a rule of property the essential principle of which had long been recognized and applied in this jurisdiction and others, including England. (*Meldon v. Devlin*, 31 App. Div. 146; *affd.*, 167 N. Y. 573 [1901]; *Parsons v. Winslow*, 16 Mass. 361, 365 [1820]; *Veazie v. Forsaith*, 76 Me. 172 [1884]; *Hagan v. Platt*, 48 N. J. Eq. 206, 207, 208 [1891]; *Greene v. Greene*, 19 R. I. 619, 621-624 [1896]; *Quinn v. First Nat. Bank*, 168 Tenn. 30 [1934]; *Matter of Nirdlinger*, 327 Penn. St. 171, 172, 173 [1937]; *Cox v. Cox*, L. R. 8 Eq. 343, 344, 345 [1869]; *Matter of Moore*, 54 L. J. Ch. 432 [1885], and see *Matter of Marshall*, 43 Misc. 238, 245 [1904].) A classical statement of the underlying principle which runs through the cases cited above was made in *Cox v. Cox*, *supra*, page 344, as follows: "The true principle in all these cases is, that neither the tenant for life nor the remainderman is to gain an advantage over the other—neither is to suffer more *damage* in proportion to *his estate and interest* than the other suffers—from the default of the obligor." (Emphasis supplied.) This was orthodox doctrine long before the decisions by this court in the *Meldon*, *Chapal* and *Otis* cases, *supra*.

In accord with that rule of property there had vested in the income beneficiary and the remaindermen respectively, prior to the effective date of section 17-c, subdivision 2, a proprietary interest in each of the properties acquired by the trustee. (*Matter of McManus*, *supra*, p. 426.)

Although the basis adopted by the courts for computing the item of interest involved differs in the various jurisdictions which have considered the question, there is a basic principle, as we have seen, which runs throughout the decisions cited above—*viz.*, that, in the income from salvage operations incidental to the administration of a trust estate, both life tenant and remainderman have a proprietary interest and both are entitled to be paid their proportionate shares thereof.

The comment made in *Matter of Rogers* (22 App. Div. 428; *affd.*, 161 N. Y. 108), by Mr. Justice Cullen—later Chief Judge of this court—applies with equal force in the case at hand where the rights of remaindermen are at stake (p. 436)—"The equities of a life tenant to receive the whole



income that may accrue during his tenancy are every whit as great as that of the remaindermen to have the *corpus* of the trust preserved unimpaired. \* \* \* *Why should each not have exactly his own, so far as it is possible to ascertain it?*" (Emphasis supplied.)

A marked difference should be noted between the provisions of section 17-c, subdivision 2, with which we are here concerned, and subdivision 1 of the same section. Unlike subdivision 2, the Legislature was careful in subdivision 1 to make its mandates in effect prospective—not retroactive. It also employed language by which its mandates would in no event conflict with any contrary intention which might be expressed by the creator of the trust.

The resultant effect of section 17-c, subdivision 2, is to transfer, without the right of recoupment, from the principal account of a trust to the income account, an amount—fixed arbitrarily and without regard to the demands of justice and equity in the circumstances at three per cent per annum computed upon the principal amount of each salvaged mortgage. Such a mandatory transfer to the life tenant of property rights which had become vested in the remaindermen under a rule of property which antedated the enactment of section 17-c, subdivision 2, transcends the Legislature's power. "Legislation which impairs the value of a vested estate is unconstitutional." (*Matter of Pell*, 171 N. Y. 48, 52, 53; *People v. O'Brien*, 111 N. Y. 1, 57-59; *Westervelt v. Gregg*, 12 N. Y. 202, 212.) As I view the statute it authorizes, without due process of law, the taking of property rights which became vested in the remaindermen under an established rule of property prior to the effective date of the statute. To that extent it violates the Fourteenth amendment to the Federal Constitution and article 1, section 6, of the Constitution of the State of New York.

I pass now to a phase of the problem which I think cannot be ignored. The questions of apportionment with which subdivision 2 of the statute attempts to deal are essentially judicial questions. This subject was examined by Story in his *Equity Jurisprudence*. ([2d ed.] vol. 1, § 489 *et seq.*) Stressing the "beneficial operations of courts of equity \* \* \* upon this confessedly intricate subject," he said:



"Without some proceedings, in the nature of an account before a Master, there would be no suitable elements upon which any court of justice could dispose of the merits of such cases." In like vein it was said by Judge Loughran writing for this court in *Matter of Otis, supra* (p. 115), that "• • • a general rule for such situations cannot be attained at a bound, that *no rule can be final for all cases* and that any rule must in the end be shaped by considerations of business policy." (Emphasis supplied.) Subdivision 2 of the statute attempts to override all this by saying that *in every case* the life tenant must at all events immediately and finally receive net income at a rate arbitrarily fixed by the statute at three per cent—no matter what may be the cross-equities of the parties and without regard for the business risks of the particular salvage operation. To this extent, subdivision 2 of the statute makes it mandatory that the court shall adjudicate every "pending proceeding or action for an accounting" without affording the parties any opportunity to be heard. The draftsmen of the statute apparently recognized some difficulty on that score, for the statute says: "Only *equitable* adjustments and balances *as between the parties* are intended to be effectuated by the provisions of this subdivision" [2]. (Emphasis supplied.) We have, then, this extraordinary situation: While subdivision 2 of the statute has not changed the law that pending questions of apportionment are to be decided upon equitable principles, yet it declares that such principles must be applied by the courts, not according to the judicial judgment of what is equitable in the circumstances of a pending controversy, but according to a legislative mandate rigidly enjoined for all pending cases.

The Legislature has no power so to declare the law "for the information and government of the courts in the decision of causes before them." (Kent, Ch. J., in *Dash v. Van Kleeck*, 7 Johns. 477, 508, 509.) In this connection it should be observed that subdivision 2 of the statute is not emergency legislation; it invokes neither the general welfare nor any other consideration of public policy. In the only opinion written below, it is said: "The Legislature has done no more in formulating a modification of existing rules than

the courts themselves could do. \* \* \*." (175 Misc. 1044, at p. 1050.) Such a proposition is not free from risk. Nobody knows what economic chaos may follow the present war. I am not prepared to say that as to all pending cases the Legislature may do at one stroke whatever courts of justice may do in accord with their tradition to proceed only in a particular controversy and only after taking evidence at a hearing held upon issues defined by pleadings. The Legislature can no more exercise judicial power than our courts can exercise legislative power. (See opinion by Ruffin, C. J. in *Hoke v. Henderson*, 25 Amer. Dec. p. 686 [N. C.].) The determination of rights of property *inter partes* is always a judicial question. As I view it, subdivision 2 of section 17-c of the Personal Property Law is a void attempt by the Legislature to make such a determination. I am led by these considerations to dissent and vote for a modification of the Surrogate's decree accordingly.

LOUGHRAN, J: (dissenting). I add a few words to the dissenting opinion of Judge Lewis in which I concur entirely.

The crux of the prevailing opinion is this striking sentence: "A statutory rule of administration which requires the trustee to apportion income in accordance with a fixed standard which in the exercise of administrative discretion the trustee would even without the statute have power to adopt does not, in our opinion, constitute a taking of property." I cannot assent to so free an appraisal of the retroactive mandate of the Legislature.

No authority is cited to show that it was always open to trustees of their own motion to pay net income to a life tenant at such a "fixed standard," in peremptory disregard of the recoupment rights of remaindermen. Indeed the general understanding of the profession appears to have been the other way, seeing that the Surrogates who devised the statute have vouchsafed us one reason alone for its enactment, *viz.*, "Trustees have hesitated to pay such net income because in the case of overpayment to the life tenant, the trustee might be surcharged with that amount." (See L. 1940, p. 1182.)

This recognition by trustees of the conflicting rights of remaindermen was not without justification. It is true that

hitherto a trustee for a life tenant and remaindermen was entitled to distribute surplus income in his discretion. (*Matter of Otis*, 276 N. Y. 101, 115.) But that discretion was always to be exercised by a trustee with reasonable judgment and with an even hand between the life tenant and the remaindermen in the particular circumstances. (See *Carrier v. Carrier*, 226 N. Y. 114, 125, 126; 28 Halsbury's Laws of England [1st ed.] 123, 124; 2 Scott on The Law of Trusts, § 187; 4 Pomeroy on Equity Jurisprudence, [5th Ed.] § 1062a.) The retroactive provisions of the statute direct trustees instantanor to make final payment of net income to a life tenant not at a fixed rate merely, but at the expense of the remaindermen if need be. Hence I cannot accept the presupposition that the statute confers no new power upon trustees.

There is no occasion now for examination of the real nature of the equitable right of a trust beneficiary. At least the beneficiary owns the obligation of the trustee—a thing which is as truly the subject-matter of property as any physical object. (See Ames, Lectures on Legal History, p. 262. Cf. 1 Scott on The Law of Trusts, § 130.) Consequently I see no warrant for the view that the respective interests of beneficiaries of a discretionary trust are not rights of property in the constitutional sense. (See *Pritchard v. Norton*, 106 U. S. 124, 132.)

LEHMAN, Ch. J., RIPPEY, CONWAY and DESMOND, JJ., concur with FINCH, J.; LEWIS and LOUGHRAN, JJ., dissent in separate opinions in which both concur.

Order affirmed, etc.

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# Supreme Court of the United States

OCTOBER TERM, 1943.

No. 52.

WILLIAM J. DEMOREST, JR., ANN DEMOREST  
and CAROLYN DEMOREST by GERALD P.  
CULKIN, their Special Guardian,

*Appellants,*

AGAINST

CITY BANK FARMERS TRUST COMPANY, as  
Trustee under the Will of HENRY C. WEST, De-  
ceased, *et al.*

APPEAL FROM THE SURROGATE'S COURT, NEW YORK  
COUNTY, STATE OF NEW YORK.

Brief of Special Guardian for Infant Appellants.

FRANCIS J. MAHONEY,  
*Counsel for the Appellants.*

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# Supreme Court of the United States

OCTOBER TERM, 1943.

No. 52.

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WILLIAM J. DEMOREST, JR., ANN DEMOREST and CAROLYN  
DEMOREST by GERALD P. CULKIN, their Special Guardian,  
*Appellants,*

vs.

CITY BANK FARMERS TRUST COMPANY, as Trustee under  
the Will of HENRY C. WEST, Deceased, *et al.*

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**Brief of Special Guardian for Infant Appellants.**

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**Reference to Official Reports of Opinions.**

Opinion of Surrogate James A. Foley, 175 Misc. 1044;

Majority opinion of Court of Appeals, 289 N. Y. 426;

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**Statement of Grounds on Which Jurisdiction of This  
Court Is Invoked.**

This appeal is from an order of the Court of Appeals of the State of New York, dated the 15th day of January, 1943, and filed on remittitur in the office of the Clerk of the Surrogate's Court, New York County, on January 25th, 1943, which affirmed an order of the Appellate Divi-

sion, First Department, which in turn had affirmed a decree of the Surrogate's Court, New York County, judicially settling the intermediate account of proceedings of the trustee above named, and directing distribution of income from salvage operations. The special guardian-appellant appeals from the order insofar as it holds that Section 17c, Subdivision 2 of the Personal Property Law of the State of New York whose provisions apply to estates of persons who predeceased the enactment of the statute and whose estates were in the process of administration prior to the enactment of the law, is constitutional (R. 87). Appellant contends that said Subdivision 2 of said statute violates the Fourteenth Amendment of the Constitution of the United States of America, because it is retroactive and deprives appellants of property without due process of law and deprives appellants of rights guaranteed to them by said Fourteenth Amendment.

### **Statement of Case.**

The above-named deceased, died on the 1st day of May, 1934, a resident of the County and State of New York. His will, dated December 14th, 1928, was admitted to probate by the Surrogate's Court, New York County on May 28th, 1934 (R. 26). In and by his Last Will and Testament (R. 90), he created a primary trust of his residuary estate for the benefit of his wife, Emma M. West, for her life or until she should remarry, certain secondary life estates, and directed the disposition thereafter to designated remaindermen. The wards of the Special Guardian are interested in the remainder (R. 91).

The executor qualified as trustee and as such received as part of the property constituting said trust, nine certain parcels of real property, which had been acquired by

the trustee while it was executor. The acquisition of these properties was through foreclosure or deed in lieu of foreclosure of mortgages which had constituted part of the original estate of the decedent (R. 31 and 32). It is unnecessary to enumerate the street addresses or to otherwise described these parcels (they are described by street address at R. 31 and 32) except to say that all the properties were improved and that two of the parcels, to wit: 168 Morrison Avenue, West New Brighton, Staten Island and 41 Montrose Avenue, Brooklyn, were resold by the trustee prior to the enactment of Section 17c of the Personal Property Law and that the other seven parcels are still held by the trustee and are the subjects of continuing salvage operations. Insofar as the parcels sold by the trustee prior to the enactment of the statute are concerned, the special guardian-appellant has no complaint with that portion of the decree affirmed which holds that the statute does not apply (R. 26). It was and is his contention that the Surrogate, the Appellate Division and the Court of Appeals correctly held that the salvage operations with respect to these parcels were completed, that the entry of a decree was not necessary to the completion of salvage operations and that these parcels and the profits thereof remained unaffected by the provisions of the statute and are subject to the law as it existed prior thereto.

The subdivision of the statute involved, to wit, Section 17c, Subdivision (2), Personal Property Law, as enacted, effective April 13, 1940, reads as follows:

"2. The existing rules of procedure applying to salvage operations respecting existing mortgage investments are continued except as modified by the subparagraphs hereinafter set forth. The terms and rules of procedure of this subdivision shall

apply specifically (a) to the estates of persons dying before its enactment and (b) to mortgages on real property held by a trustee under a deed of trust or other instrument executed before the date of its enactment and (c) to real property acquired by foreclosure of mortgage or real property acquired in lieu of foreclosure before or after the date of its enactment, in trusts created or mortgage investments made prior thereto, and (d) to any pending proceeding or action for an accounting of the transactions of an executor or trustee.

(a) Net income during the salvage operation up to three per centum per annum upon the principal amount of the mortgage shall be paid to the life tenant, regardless of principal advances for the expenses of foreclosure or of conveyance in lieu of foreclosure and arrears of taxes and other liens which occurred prior to such foreclosure or conveyance and the cost of all capital improvements. Any payment of net income heretofore or hereafter made to the life tenant up to such three per centum per annum shall be final and shall be not subject to recoupment from the life tenant or as a surcharge against the trustee or executor. The amount of all such payments shall be taken into account, however, in the apportionment of the proceeds of sale and shall be charged against the share of the life tenant.

(b) The foregoing principal advances shall be repaid out of excess net income above such three per centum per annum. When principal advances have been satisfied, any excess income shall be impounded (subject to reinvestment under the terms



of the will or deed) to await sale and apportionment.

(c) The unpaid principal advances shall be a primary lien upon the proceeds of sale and shall be paid first out of any cash so derived. If insufficient the balance shall be a primary lien upon any purchase money mortgage received upon the sale.

(d) The purpose of the enactment of this subdivision is declared to be the simplification of the rules of procedure in mortgage salvage operations and the elimination of present complications which work to the disadvantage of the life tenant, who is usually the principal object of the testator's or settlor's bounty, by depriving him of a fixed right to the actual payment of any net income earned by the property. Such fixed right is granted in lieu of the discretion now given to the trustee to pay net income or any part thereof to the life tenant. The general rules of the apportionment of the proceeds of sale between life tenant and remainderman are retained subject to the express modifications made herein. Only equitable adjustments and balances as between the parties are intended to be effectuated by the provisions of this subdivision. If any provision of this subdivision or the application thereof to any mortgage or acquired property by foreclosure or conveyance, or to any trust is held invalid, the remainder of the subdivision and the application of such provision to any other mortgage or property acquired by foreclosure or conveyance or other trust shall not be affected thereby."

### **Specification of Assigned Error Intended to Be Urged.**

The Court of Appeals erred in holding:

1. That 17c of the Personal Property Law of the State of New York (Chap. 452 of the Laws of New York 1940) as applied to the trust created under the Will of Henry C. West and to its administration, was not repugnant to the Fourteenth Amendment of the Constitution of the United States.
2. That said statute and its application, by the decree appealed from, to the Estate of Henry C. West, did not deprive appellants of property and of vested rights without due process of law.

### **POINT I.**

**Subdivision 2 of Section 17-c of the Personal Property Law of the State of New York is unconstitutional because it is retrospective and deprives the remaindermen of vested rights without due process of law.**

At the outset, this appellant desires to make it clear that he is not unsympathetic with the purpose actuating the sponsors of the legislation and that he is not unmindful of the fact that situations have developed and are presently continuing with respect to salvage operations which merit some consideration on behalf of life tenants in many instances. The complaint of this appellant is not with subdivision 1 which applies only to the estates of persons dying or trusts created after the effective date of the statute, but with the method pursued in the attempt to accomplish relief retroactively, and his sympathy cannot permit him to overlook the violation of constitutional

rights which results from the enactment and application of subdivision 2 of this section.

Subdivision "2" of the statute provides that the "terms and rules of this subdivision shall apply specifically (a) to the estates of persons dying before its enactment and (b) to mortgages on real property held by a trustee under a deed of trust or other instrument executed before the date of its enactment and (c) to real property acquired by foreclosure of mortgage or real property acquired in lieu of foreclosure of mortgage before or after the date of its enactment in trusts created or mortgage investments made prior thereto, and (d) to any pending proceeding or action for an accounting of the transactions of an executor or trustee."

Subdivision "2(a)" directs the immediate payment to the life tenant out of net income from the realty at the rate of 3% per annum of the face amount of the mortgage beginning with the date of the acquisition of the real property by the trustee and continuing to the resale of the formerly mortgaged property, regardless of advances made from principal for expenses of foreclosure or of a conveyance in lieu of foreclosure, and regardless of the costs of capital improvements. This subsection further provides that any such payments shall be final and not subject to recoupment from the life tenant and shall be taken into account only in the apportionment of the proceeds of sale and charged against the share of the life tenant.

The purpose of the legislation, as explained in Subdivision "2(d)" thereof, is to simplify procedure in salvage operations, and to remove disadvantage to life tenants under the discretionary power given to the trustee under the Chapal-Otis Rules (*Matter of Chapal*, 269 N. Y. 464 and *Matter of Otis*, 276 N. Y. 101; 277 N. Y. 659) to disburse income to the life tenant, after advances made

from principal as an incident to the acquisition of the property have been repaid. Concededly the trustee had such power before the enactment of Section 17-c, subject to accounting and subject to recoupment in the event of inequitable allocation. This subdivision states also that "the life tenant is usually the principal object of the testator's or settlor's bounty" and that under the Chapal-Otis rules, the beneficiary intended to be most favored was thus deprived of income during the salvage period. Subsection 2(b) provides that the surplus income above said 3% shall be applied to the advances made from principal, for arrears of taxes, other liens and the acquisition and the management of the property, until all of such advances have been satisfied.

Subdivision 2 is expressly retroactive and no party to this appeal will attempt to dispute this fact. Its express purpose is to affect acts which occurred and such rights as may have accrued by application of the Chapal-Otis rules prior to April 13, 1940, the effective date of the statute.

Concededly all the parcels of real estate involved in the case at bar were acquired by the trustee through foreclosure or deed in lieu of foreclosure prior to the enactment of the statute and the seven unsold parcels were, prior to the statute, and still are, subjects of salvage operations.

Certain observations inescapably present themselves to the mind of this appellant. The first is the ease with which the statute subordinates the remainderman to the life tenant; and the second, that the legislature has interpreted the intent of each and every testator who died prior to the enactment of the statute, and whose estate contained a salvage operation.

By the law of the State of New York, fixed by determination of its highest court prior to the enactment of

the disputed section, proceeds from transactions of fiduciaries in salvage operations affected the rights of remaindermen and life tenants because the mortgages were "security not for principal alone but for income as well" (*Matter of Chapal*, 269 N. Y. 464, 472). Therefore, as stated by Lewis, J. in one of the dissenting opinions of the Court of Appeals (R. 124 to 126):

"When the properties here involved came into the hands of the trustee, the rule of apportionment last quoted above was not a matter of grace as the majority opinion herein [fol. 258] seems to hold. It was a rule of property the essential principle of which had long been recognized and applied in this jurisdiction and others, including England. (*Meldon v. Devlin*, 31 App. Div. 146; *affd.*, 167 N. Y. 573 [1901]; *Parsons v. Winslow*, 16 Mass. 361, 365 [1820]; *Veazie v. Forsaith*, 76 Me. 173 [1884]; *Hagan v. Platt*, 48 N. J. Eq. 206, 207, 208 [1891]; *Greene v. Greene*, 19 R. I. 619, 621-624 [1896]; *Quinn v. First Nat. Bank*, 168 Tenn. 30 [1934]; *Matter of Nirdlinger*, 327 Penn. St. 171, 172, 173 [1937]; *Cox v. Cox*, L. R. 8 Eq. 343, 344, 345 [1869]; *Matter of Moore*, 54 L. J. Ch. 432 [1885], and see *Matter of Marshall*, 43 Misc. Rep. 238, 245 [1904].) A classical statement of the underlying principle which runs through the cases cited above was made in *Cox v. Cox*, *supra*, page 344 as follows: 'The true principle in all these cases is, that neither the tenant for life nor the remainderman is to gain an advantage over the other—neither is to suffer more damage in proportion to his estate and interest than the other suffers—from the default of the obligor.' (Emphasis supplied.) This was orthodox doctrine long before the decisions by this

court in the *Meldon, Chapal* and *Otis* cases, *pra.* In accord with that rule of property there had vested in the income beneficiary and the remaindermen respectively, prior to the effective date of section 17-c, subdivision 2, a proprietary interest in each of the properties acquired by the trustee. (*Matter of McManus, supra*, p. 426.)

Although the basis adopted by the courts for computing the item of interest involved differs in the various jurisdictions which have considered the question, there is a basic principle, as we have seen, which runs throughout the decisions cited above—viz., that, in the proceeds from salvage operations incidental to the administration of a trust estate, both life tenant and remainderman have a proprietary interest and both are entitled to be paid their proportionate shares thereof.

A marked difference should be noted between the provisions of section 17-c, subdivision 2, with which we are here concerned, and subdivision 1 of the same section. Unlike subdivision 2, the Legislature was careful in subdivision 1 to make its mandates in effect prospective—not retroactive. It also employed language by which its mandates would in no event conflict with any contrary intention which might be expressed by the creator of the trust.

[fol. 259] The resultant effect of section 17-c, subdivision 2, is to transfer, without the right of reconpment, from the principal account of a trust to the income account, an amount—fixed arbitrarily and without regard to the demands of justice and equity in the circumstances at three per cent. per annum computed upon the principal amount of each salvaged mortgage. Such a mandatory transfer to the life tenant of property rights which had become



vested in the remaindermen under a rule of property which antedated the enactment of section 17-c, subdivision 2, transcends the Legislature's power. 'Legislation which impairs the value of a vested estate is unconstitutional.' (*Matter of Pell*, 171 N. Y. 48, 52, 53; *People v. O'Brien*, 111 N. Y. 1, 57-59; *Westervelt v. Gregg*, 12 N. Y. 202, 212.) As I view the statute it authorizes, without due process of law, the taking of property rights which became vested in the remaindermen under an established rule of property prior to the effective date of the statute. To that extent it violates the Fourteenth amendment to the Federal Constitution and article 1, section 6, of the Constitution of the State of New York."

How can the legislature say that where the testator created a trust, without expressly stating a priority, between life tenant and remaindermen and where there has been no adjudication of intent, the primary and superior object of the testator's bounty usually was and therefore will be presumed to have been in every instance, the life beneficiary? Surely, it must be admitted that in many instances, the testamentary provision for a life tenant is more of a token or the fulfillment of a moral obligation, the primary concern of the testator being the remainderman. In fact the tendency to preserve estates was the reason for the statutes against suspensions. Many life estates are created as a minimum compliance with Section 18 of the Decedent Estate Law which requires that a surviving spouse receive not less than a stated minimum share. In the will involved in this estate, the testator believed his obligation to the life tenant to exist only so long as she does not remarry. The life tenant in many instances is unquestionably secondary. The stat-

ute summarily adjudicates the intent of every testator without any process of law and without any adjudication in the particular instance. "No will has a twin brother." This appellant is willing to make the concession, that there would be process of law, if the statute provided for protection to the life tenant, equitably distributed with protection to remaindermen, in any case where the Court of original jurisdiction shall first properly adjudicate that the life tenant was the primary object of the testator's bounty and that such protection to the life tenant was the intent of testator. This statute makes no provision for any adjudication by a court but presumes to retrospectively adjudicate generally and take unto the legislature this power of the judicial branch of the government (Story, Equity Jurisprudence 2nd Ed. Vol. 1, Sec. 489, *et seq.*). Lewis, J., in his dissenting opinion develops this point as follows:

"Subdivision 2 of the statute attempts to override all this by saying that in every case the life tenant must at all events immediately and finally receive net income at a rate arbitrarily fixed by the statute at three per cent.—no matter what may be the cross-equities of the parties and without regard for the business risks of the particular salvage operations. To this extent, subdivision 2 of the statute makes it mandatory that the court shall adjudicate every 'pending proceeding, or action for an accounting' without affording the parties any opportunity to be heard. The draftsmen of the statute apparently recognized some difficulty on that score, for the statute says: 'Only equitable adjustments and balances, as between the parties are intended to be effectuated by the provisions of this subdivision' [2]. (Emphasis supplied.) We

have, then, this extraordinary situation: While subdivision 2 of the statute has not changed the law that pending questions of apportionment are to be decided upon equitable principles, yet it declares that such principles must be applied by the courts, not according to the judicial judgment of what is equitable in the circumstances of a pending controversy, but according to a legislative mandate rigidly enjoined for all pending cases.

[fol. 260] The Legislature has no power so to declare the law 'for the information and government of the courts in the decision of causes before them.' (Kent, *Ch. J.*, in *Dash v. Van Kleeck*, 7 Johns. 477, 508, 509.) In this connection it should be observed that subdivision 2 of the statute is not emergency legislation; it invokes neither the general welfare nor any other consideration of public policy. In the only opinion written below, it is said: 'The Legislature has done no more in formulating a modification of existing rules than the courts themselves could do. \* \* \*' (175 Misc. 1044, at p. 1050.) Such a proposition is not free from risk. Nobody knows what economic chaos may follow the present war. I am not prepared to say that as to all pending cases the Legislature may do at one stroke whatever courts of justice may do in accord with their tradition to proceed only in a particular controversy and only after taking evidence at a hearing held upon issues defined by pleadings. The Legislature can no more exercise judicial power than our courts can exercise legislative power. (See opinion by Ruffin, *C. J.* in *Hoke v. Henderson*, 25 Amer. Dec. p. 686 [N. C.].) The determination of rights of property *inter partes* is always a judicial question. As I view it, sub-

division 2 of section 17-c of the Personal Property Law is a void attempt by the Legislature to make such a determination."

As stated by the Court of Appeals in *Morris v. Sickly*, 133 N. Y. 456, on the determination of testamentary intent:

"The intention and purpose must be found to exist at the time of the execution of the will, and cannot be varied or changed by any after-occurring events."

Under New York Law, the only intention which may be attributed to a testator is that which results from the natural implications of the words employed in the will when viewed in the light of the circumstances surrounding him. *Matter of Rowland*, 273 N. Y. 100 and cases cited.

It is a well established canon of statutory construction, that a retrospective law may not validly impair vested rights. A retrospective law is

" . . . a law which looks backward or contemplates the past; one which is made to affect acts or facts occurring, or rights accruing, before it came into force. Every statute which takes away or impairs vested rights acquired under existing laws, or creates a new obligation, imposes a new duty or attaches a new disability in respect to transactions or considerations already past; must be deemed retrospective." (Black's Law Dictionary, 3rd Edition, adopting the definition of Justice Story in *Society of Propagation v. Wheeler*, 22 F. Cas. No. 13,156; *Sturges v. Carter*, 114 U. S. 511, 519.)

"A retrospective law relates back to and gives to a previous transaction, some different legal effect from that which it had under the law when it occurred", *Corpus Juris*, Vol. 12, Sect. 778, *Chicago, etc. v. State*, 47 Nebr. 549; *Clarke Inst. Co. v. Wadden*, 34 S. D. 550.

Only on the theory of police power and in the face of public emergency may a retrospective law, such as the one under discussion, be passed.

In the case at bar no paramount interest of the people is at stake nor is there any question involving public health, welfare or morals. \* \* \* As said by Lehman, J. (now Chief Judge), in *Matter of People, etc. (Title & Mortgage Guarantee Co.)*, 264 N. Y. 69, 84:

"The decisions of the United States Supreme Court do certainly establish these criteria: Legislation which impairs the obligations of a contract or otherwise deprives a person of his property can be sustained only when enacted for the promotion of the general good of the public, the protection of the lives, health, morals, comfort and general welfare of the people and when the means adopted to secure the end are reasonable."

The contention that laws must be tested according to the social and economic conditions existing at the time of their enactment, cannot constitute ground for a retroactive adjudication of intent by the legislature and to excuse an adjudication as to intent of the testator by the judicial branch of the government wherein that right and duty are reposed.

"Vested rights cannot be affected by subsequent legislation." *Lytle v. Beveridge*, 58 N. Y. 592, 602;

*American Smelting Co. v. Colorado*, 204 U. S. 103;  
*McCullough v. Com.*, 172 U. S. 102.

See also, *Hathhorn v. Natural Carbonic Gas Co.*, 194 N. Y. 326; *In re Pell*, 171 N. Y. 48; *People v. Powers*, 147 N. Y. 104, 109; N. Y., etc., *R. R. Co. v. Van Horn*, 57 N. Y. 473; *Ryder v. Hulse*, 24 N. Y. 372; *Westervelt v. Gregg*, 12 N. Y. 202.

"Rights are vested when the right to enjoyment, present or prospective, has become the property of some particular person or persons as a present interest." 12 *Cor. Jur.*, 485; Cooley on Constitutional Law, page 351; *Pearsall v. Great Northern R. R. Co.*, 161 U. S. 646, 673.

Due process of law is defined as

" . . . an orderly proceeding adapted to the nature of the case, in which the citizen has an opportunity to be heard, and to defend, enforce and protect his right."

See *City of Buffalo v. Newbeck*, 209 App. Div. 386.

The "due process" clause of the Federal Constitution should be construed in the light of pre-existing law. 16 *Cor. Jur.*, Section 568 (d), page 1149. The applicable law existing prior to the enactment of Section 17-c Personal Property Law has already been discussed herein.

Obviously on April 12th, 1940, one day prior to the effective date of the statute, *Matter of Otis* and *Matter of Chapal*, *supra*, expressed the New York law on the question of allocation of income in salvage operations. In any estate involving a salvage operation settled by decree made prior to said date, the rights of principal and in-



come would have been determined in compliance with the law as fixed by said cases. A decree would and could have been entered only because rights existed. But according to Section 17c, if the salvage operation continued for two days longer, those rights became non-existent. In the case at bar, if Section 17c is applicable, the remaindermen are to receive different considerations because the trustee settled its intermediate account subsequent and not prior to the effective date of the statute. This does not seem to make sense or to possess the positiveness of law.

Section 17c of the Personal Property Law presumes to substitute a different measure of equity and to create rights in lieu of or in destruction of rights previously existing. It overlooks the definition that a salvage operation is a "joint salvage venture" (*Matter of Chapal, supra*, *Matter of Otis, supra*) and the legislature invades a province which is not its own.

The rights and obligations of joint venturers are fixed in law, those rights having been defined by the judicial branch of the government with which rests the privilege of definition. The legislature, however, in enacting Section 17c aforesaid, disregards the definition of the courts and arbitrarily revokes the rights of one joint venturer and retroactively determines the rights of another joint venturer to be at least 3% of the face amount of the mortgage previously affecting the property payable out of net income, regardless of the amount of the principal, regardless of the value of the property acquired, regardless of the costs of acquisition, regardless of the expenses for the removal of liens and regardless of the expense of renovation and repair.

In *Matter of Otis*, and *Matter of Chapal, supra*, the Court expressly states that a mortgage taken by a trustee constitutes security for principal as well as income. The

Chapal opinion reviews some of the earlier authorities and states that the rule declared in the Chapal opinion amounts to a restatement of a well established rule of property in the administration of estates and trusts.

As late as *Matter of McManus*, 282 N. Y. 420, the Court of Appeals stated unanimously that accrued income must be ratably distributed between the principal trust and the estate of a life tenant who died before the completion of the salvage operation. If the estate of the life beneficiary has a vested although unrealized right to income, principal has at least an equal right to preservation for the benefit of the remaindermen, which fact the legislature apparently overlooked in its desire to provide only for the rights of the life tenant, even to the deprivation of the trust principal. The legislature has no power to deprive an individual of private property without his consent and give it to another. As stated by the Court of Appeals in *New York & Oswego R. R. v. Van Horn*, 57 N. Y. 473, 477:

“ \* \* \* This no act of the legislature can do. It can never take the private property of one individual without his consent, and give it to another. (Citing cases.)

“Such an act comes in direct conflict with the constitutional provision that ‘no person shall be deprived of life, liberty or property, without due process of law’.”

As determined in *Matter of McManus*, *supra*, there appears to be no question that under the law of New York the rights of principal in the proceeds of salvage operations constitute property just as much as do the rights of income. That the rights of the remaindermen in the case at bar are property rights with constitutional

protection, see *Matter of Pell*, 171 N. Y. 48, 53; *Matter of Lansing*, 182 N. Y. 238; *Westervelt v. Gregg*, 12 N. Y. 202, 212. In the last mentioned case, the concurring opinion says:

“ \* \* \* No power in the State can legally confer upon one person or class of persons, the property of another person or class without their consent whatever motives or policy may exist in favor of such person.”

In *Matter of Pell* the Court of Appeals said:

“A right of succession passed to the four living children of George at the death of testator. It came from him, it was transferred by him, taking effect at his death; and passed then or never. But the right itself, although vesting in the successors at once, had its own peculiar character. It could not ripen into possession or enjoyment until the death of the life tenants, and before that event was contingent solely as to the person who should eventually take and the proportions to be observed. The legatees as a class were certain; the particular individuals alone uncertain. \* \* \* To say that no beneficial interest passed into the hands where it was taxable is very different from saying that no beneficial interest passed at all. The doctrine of the case (*Matter of Curtis*, 142 N. Y. 219) and its manifest trend was that where the particular persons who were to have the beneficial possession were uncertain, the appraisal and collection must be adjourned until the uncertainty ended, but no new doctrine of the passing of the right of succession at a date later than that of the will was at all

asserted. It is said, however, that the right of succession passing in remainder by the will was at best merely technical and nominal, and that the beneficial interest did not pass until the termination of the life estate. In one sense that is true. The right of succession to specific individuals might prove barren, and for that reason the claim of the state should be adjourned, and the law of 1892 fully recognizes and provides for such an adjournment, but a necessary and admissible delay in appraisal and collect is a very different matter from an assertion that no beneficial right of succession passed at all until after the decease of the life tenants."

Even a contingent remainder constitutes a right of property which may not be impaired or destroyed by a statute passed after its creation. *Aetna Life Insurance Company v. Hoppin*, 214 Fed. 928.

We quote as follows from *Matter of Lansing*, 182 N. Y. 238, 243:

"Mrs. McVickar was born before her grandfather died, and upon his death she took a vested interest in remainder \* \* \*"

It is argued by the sponsors of the objectionable statute that there is no change in the computation of the respective interests of income and principal under the formula set forth in *Matter of Chapal, supra*, and *Matter of Otis, supra*. It is contended by said sponsors that the new section merely releases income to the life tenant but does not increase the ultimate amount payable to the respective interests on the ultimate sale of the property. With this contention appellant does not agree. The bases for his disagreement are set forth in Point II of this

brief. The equality of the statutory rule with the Chapal-Otis Rule is more of appearance than of fact. There is equality where the proceeds of sale are sufficient to reimburse all of the advances made out of principal and to leave a surplus. However, when the sponsors of the legislation contend, upon which contention the legislature presumably relied, that there is equality, they overlook the fact that such a result will not apply in every instance. Keeping abreast of economic conditions, the court will recognize the fact that because of depressed values, high assessed valuations with resulting excessive taxes, requirements of the multiple dwelling law of New York and "a buyers' market", mortgagees are often unable to collect anything on their mortgages and in many instances property has been abandoned because of the impossibility of procuring from the property even the cost to make the same legally tenantable. It must be further borne in mind that the statute does not limit its provisions to first mortgages, but applies as well to subordinate mortgage liens and the history of these in the City of New York is too well known to require further comment.

Application of the statute guarantees all net income to the life tenant except to the extent such income exceeds 3%, not of the value of the property, but of the face amount of a mortgage which no longer exists. All loss is taken from principal even to the extent that no portion of the 3% can be reclaimed should the completion of the salvage operation show that the aggregate of the payments to income exceeds the amount to which income, as a joint venturer, was entitled.

As stated by Loughran, J., in his dissenting opinion below (R. 128):

"The crux of the prevailing opinion is this striking sentence: 'A statutory rule of adminis-

tration which requires the trustee to apportion income in accordance with a fixed standard which in the exercise of administrative discretion the trustee would even without the statute have power to adopt does not, in our opinion, constitute a taking of property.' I cannot assent to so free an appraisal of the retroactive mandate of the Legislature.

No authority is cited to show that it was always open to trustees of their own motion to pay net income to a life tenant at such a 'fixed standard', in peremptory disregard of the recoupment rights of remaindermen. Indeed, the general understanding of the profession appears to have been the other way, seeing that the Surrogates who devised the statute have vouchsafed us one reason alone for its enactment, viz., 'Trustees have hesitated to pay such net income because in the case of overpayment to the life tenant, the trustee might be surcharged with that amount.' (See L. 1946, p. 1182.)

This recognition by trustees of the conflicting rights of remaindermen was not without justification. It is true that hitherto a trustee for a life tenant and remaindermen was entitled to distribute surplus income in his discretion. (*Matter of Otis*, 276 N. Y. 101, 115.) But that discretion was always to be exercised by a trustee with reasonable judgment and with an even hand between the life tenant (fol. 261) and the remaindermen in the particular circumstances. (See *Carrier v. Carrier*, 226 N. Y. 114, 125, 126; 28 Halsbury's Laws of England [1st ed.], 123, 124; 2 Scott on The Law of Trusts, Sec. 187; 4 Pomeroy on Equity Jurisprudence, [5th ed.] Sec. 1062a.) The retroactive provisions of the statute direct trustees instant



to make final payment of net income to a life tenant not at a fixed rate merely, but at the expense of the remaindermen if need be. Hence I cannot accept the presupposition that the statute confers no new power upon trustees.

There is no occasion now for examination of the real nature of the equitable right of a trust beneficiary. At least the beneficiary owns the obligation of the trustee—a thing which is as truly the subject-matter of property as any physical object. (See Ames, Lectures on Legal History, p. 262. Cf. 1 Scott on The Law of Trusts, Sec. 130.) Consequently I see no warrant for the view that the respective interests of beneficiaries of a discretionary trust are not rights of property in the constitutional sense. (See *Pritchard v. Norton*, 106 U. S. 124, 132.)”

As hereinbefore stated, equitable powers rest with the Court and any argument that the legislature has done what the Court might have done under certain and proper conditions, overlooks the fact that the legislature and the judiciary are separate branches of government and that, whereas the courts may apply equity in a particular instance, on adjudicated facts, the legislature has no inherent power to adjudicate or establish rules of property and of law changing the pre-existing rights of property.

The fact, if such fact can be presumed, that in the instant case the statute might be reasonable in its provisions and work no hardship, is not an argument to support the validity of the statute. It is the duty of the courts to declare invalid an unconstitutional statute no matter how desirable or beneficial the attempted legislation may be. 16 Cor. Jur. Sec. 92 and cases cited.

As said by the Court of Appeals in *City of Rochester v. West*, 164 N. Y. 510, 514:

"The validity of a statute is not to be determined by what has been done in any particular instance; but by what may be done under it. (*Stuart v. Palmer*, 74 N. Y. 183; *Gilman v. Tucker*, 128 N. Y. 190, 200.) It is equally true that the validity of a statute or ordinance is not to be determined from its effect in a particular case, but upon its general purpose and its efficiency to effect that end."

It may be that the life tenant is usually the primary object of testator's bounty but, as hereinbefore stated, the test of constitutionality is not to be determined from the effects in a particular case but upon the general purpose of a statute and its efficiency to effect that end. Since the enactment of Section 18, Decedent Estate Law, which deprived a testator or testatrix of the power to disinherit a surviving spouse, many instances have come to the attention of practitioners where the testator or testatrix is unhappily married or separated from his or her spouse and creates a life estate as a minimum compliance with the statute. It is reasonable to state that hardly a practicing attorney in the State of New York has failed, in the last ten years, to come in contact with a client who created a life estate for a surviving spouse at the same time hoping that he or she would never enjoy a penny of it. Every practicing attorney knows and every judge knows of at least one instance in his experience where a testator was more concerned about his remaindermen than he was about the life tenant. In none of these instances can it reasonably be maintained that the testator was primarily concerned with the life tenant.

Applying the test heretofore quoted from *City of Rochester v. West, supra*, the application of Section 17-c of the Personal Property Law would not comply with the wishes of the testator in the instances mentioned but would be absolutely in opposition to such wishes. It is for this reason that appellant stated *supra*, that there might be validity to the statute if it provided first for an adjudication of the intent of the testator, and if the Court should first adjudge the intent of the testator, which could be gleaned from his will, the facts surrounding the making of his will, his life or association with and regard or affection for the life tenant, then, upon the basis of such adjudication, the intent could be carried out by giving to the life tenant, the preference which the testator intended. The legislature had no right to create retroactively one category for all last wills and testaments which involve life estates.

## POINT II.

The statute, in directing the ascertainment of net income on a fiscal year basis commencing with the anniversary date of acquisition of title, as construed by the decree appealed from, directing income payments at a specified rate and making said provisions retroactive, is unconstitutional.

As argued in Point I, the legislative branch of government has no power under the constitution to enact retroactive laws which deprive a person or persons of vested rights which have accrued under and pursuant to the law as it existed at the time the statute was enacted. The test of constitutionality is whether the statute results in deprivation of rights in any instance where the statute is applicable. To demonstrate simply that the applica-

tion of the statute results in deprivation of rights of remaindermen, we will compare the preexisting law with the statutory provisions. We will presume a set of facts to demonstrate how the application of the statute can result in such deprivation. As any language or reasoning of the author of this brief would be but a poor substitute, we will use the language of Mr. Surrogate Delehanty in *Matter of Wacht*, New York Law Journal, January 14th, 1942.

Concededly *Matter of Chapal, supra* (cited and followed in *Matter of Otis, supra*), fixed the pertinent law as it existed when the statute was enacted. In *Matter of Chapal* at page 472 a unanimous court (excepting O'Brien, J., not sitting) spoke through Loughran, J., as follows:

" . . . If the income of a particular parcel is more than sufficient to pay the carrying charges thereof, the trustees are hereby directed to exercise their own discretion and judgment with respect to distributing such surplus income entirely or to retaining the same or some part thereof to meet possible subsequent deficiencies. If such surplus exists in the case of a particular parcel as to which the trustees have theretofore taken or applied funds from the principal of the trust estate to pay deficiencies of income, the trustees are directed to reimburse the principal of the trust estate from such surplus income."

Section 17-c of the Personal Property Law, subdivisions 2 (a), (b) and (c) provide as follows:

"(a) Net income during the salvage operation up to three per centum per annum upon the principal amount of the mortgage shall be paid to the life tenant, regardless of principal advances for the

expenses of foreclosure or of conveyance in lieu of foreclosure and arrears of taxes and other liens which occurred prior to such foreclosure or conveyance and the costs of all capital improvements. Any payment of net income heretofore or hereafter made to the life tenant up to such three per centum per annum shall be final and shall be not subject to recoupment from the life tenant or as a surcharge against the trustee or executor. The amount of all such payments shall be taken into account, however, in the apportionment of the proceeds of sale and shall be charged against the share of the life tenant.

(b) The foregoing principal advances shall be repaid out of excess net income above such three per centum per annum. When principal advances have been satisfied, any excess income shall be impounded (subject to reinvestment under the terms of the will or deed) to await sale and apportionment.

(c) The unpaid principal advances shall be a primary lien upon the proceeds of sale and shall be paid first out of any cash so derived. If insufficient the balance shall be a primary lien upon any purchase money mortgage received upon the sale."

We quote as follows from *Matter of Wacht, supra*:

"The statute says that the 'amount of all such payments (to income) shall be taken into account, however, in the apportionment of the proceeds of sale and shall be charged against the share of the life tenant.' This provision of the statute contemplates of course that there shall be in existence

a share of the life tenant in excess of the amount irrevocably paid. Where there is no share of the life tenant against which the payments can be charged the statutory rule for charge is a futility. An assumed state of facts respecting a first mortgage salvage operation will illustrate the vice of the statute even in the case of a prior lien. We will assume that a mortgage of \$10,000 bearing interest at five per cent. is unprotected by the moratorium laws. On its due date all of the interest is paid up fully. The owner of the equity cannot pay the principal. On the mortgage due date a tax bill of \$500 becomes due. The owner delivers a deed to the estate fiduciary in lieu of foreclosure and receives for it the sum of \$500. The fiduciary thereupon pays the tax bill and begins the salvage operation. New money has been used to the extent of \$1,000 and principal is then involved in the salvage operation to the extent of \$11,000. There is no accrued and unpaid income due to income account at the beginning. During the salvage operation which lasts four years the net earnings per year are exactly \$300. Since these earnings equal exactly the statutory rate to which the life tenant is entitled on the original principal sum of \$10,000 the estate fiduciary pays the money over to income account. On the fourth anniversary of acquisition of the fee the fiduciary sells it for \$7,000. He promptly reimburses principal for the \$1,000 of new money which was advanced in the salvage operation. There is left in the fiduciary's hands \$6,000 and he is obliged to apportion the salvage proceeds under the statute. He knows that principal now has a \$10,000 interest and that income has a \$2,000 interest computed by multi-



plying by 4 (the number of years of the salvage operation) the sum of \$500 (the amount of interest at the mortgage rate to be credited to the income account). The denominator of the apportionment fraction is 12,000, the numerator for principal is 10,000 and that for income 2,000. Obviously principal takes five-sixths of the salvage proceeds and income one-sixth. The apportionable salvage proceeds consist of \$7,000 received for the fee less \$1,000 refunded for new advances, plus the \$1,200 earned during administration. Thus the apportionable salvage proceeds are \$7,200. Income is entitled to one-sixth, or \$1,200, which is the precise amount that income had received during the operation. Principal is entitled to \$6,000, which is the precise amount due it under the Chapal-Otis rule.

But what if the \$7,000 sale price was gross and not net? If we vary the statement by assuming that the brokerage on the sale, the attorneys' fees and other expenses of sale used up \$600, we then find that the net sale proceeds are \$6,400. As before, principal account is paid \$1,000 in refund of the new money. This leaves in the fiduciary's hands \$5,400. Just as before, the fiduciary must make an apportionment between principal and income. The fractions of interest remain exactly the same, five-sixths and one-sixth. The fiduciary adds to the net sale proceeds after refund of new money—\$5,400—the profits during operation—\$1,200—and gets an apportionable total of \$6,600. He takes five-sixths of this for principal account and finds that he should have in principal account \$5,500. In fact the total in his hands is only \$5,400. He knows of course that the missing \$100 is in the hands of

the income beneficiary whose share of one-sixth of the salvage proceeds was only \$1,100. Though the income beneficiary has been paid \$1,200 under the statute the fiduciary cannot recover the excess payment of \$100. The remaindermen will not be content to suffer such a loss.

It is a simple task to select many states of fact in salvage operations which produce like proof of the invalidity of the statute. One other example will be given. A salvage operation is undertaken in respect of a six per cent. first mortgage of \$10,000. At the date of acquisition in foreclosure two years' interest is in default, as well as two years' taxes amounting to \$1,200. The cost of foreclosure is \$600. This amount plus the amount needed to pay the taxes aggregates \$1,800 of new money which principal account must advance. After completing the foreclosure the trustee operates the property for eighteen months and has a net yearly return of \$600. The operation produces \$900 net during the eighteen months. If the statutory income share is to be computed ratably on a portion of a year, income would be entitled to have paid currently as earned the sum of \$450 which is three per cent. per year on \$10,000 for eighteen months. If, on the other hand, the statutory scheme of payment is to compel payment to income of the first money earned up to three per cent., then, the \$300 earned during the six months of the second year of operation would all be payable to income and thus income would get one-half of the first year's operation and all of the second year's operation, or a total of \$600. On the assumption that the statutory rule provides for a ratable sharing of the income the amount paid to income is assumed

to be \$450. On that assumption \$450 is left as a balance of earnings during operation. This amount is credited upon the \$1,800 of new moneys advanced and leaves a balance of \$1,350 to be collected out of sale proceeds, if at all. On this state of facts income has an income credit in the salvage apportionment of \$2,100—six per cent. on \$10,000 for a total of three and one-half years. Principal for apportionment purposes has an interest of \$10,000. The fraction for apportionment has the denominator 12,100. The numerator for principal account is 10,000 and for income account is 2,100.

The sale proceeds after deducting the immediate expenses of the sale are \$2,750.00. The net proceeds of operation are \$900.00. The gross salvage proceeds are \$3,650.00. Against this total is to be charged the new capital advances of \$1,800. This leaves a balance to apportion of \$1,850.00. Out of the total sum to be apportioned there is to be paid to income account ( $21/121 \times 1850$ ) a total of \$321.07. The balance payable to principal ( $100/121 \times 1850$ ) is \$1,528.93.

On the assumption that the statutory rule for payment to income account required a payment of only \$450.00 and on the assumption that income account is entitled on apportionment only to a total of \$321.07 it is obvious that income has been *irretrievably overpaid* \$128.93. The trustee receives in the course of the salvage operation the sale proceeds of \$2,750.00 and the operation proceeds of \$900.00, making a total of \$3,650.00. He pays to income account under the statute prior to sale a total of \$450.00. He refunds to principal account out of the proceeds of operation another \$450.00. He pays the balance of new money due to principal

out of the sale proceeds and thus appropriates \$1,350.00. The total of these three items is \$2,250.00. Leaving in the hands of the trustee a balance of only \$1,400.00.

Since principal (after full repayment of capital advances amounting to \$1,800) is entitled to an apportioned share amounting to \$1,528.93 it is obvious that it is short by \$128.93—the *non-recoverable* overpayment to income.

In the operation as stated income received irrevocably under the statute a sum of \$128.93 belonging to principal. If the statutory formula operates to give income the whole \$300 which was earned during the six months of the second year of operation (rather than \$150 thereof), then the overpayment to income is increased by \$150 to \$278.93.

The two salvage operations which have been supposed by the court show that the likelihood of a gross overpayment to income under the statute is very grave in any instance where only earnings during operation (as in the case of a junior lien) furnish the fund to be apportioned. These examples also show that only if the earnings during operation are so large as to make the statutory payments therefrom to income negligible or if the sale price is high or if income's participation in the salvage is very large or if some permutation of these factors exists which favors the statute will the rights of the parties under the statute agree with their rights under the settled law of the state declared in *Matter of Chapal* and *Matter of Otis* (*supra*). A statute with so many infirmities cannot be sustained.

If attempt be made to salvage the statute by saying that it is applicable only to those salvage

operations in which the combined sale and operation proceeds do furnish an interest payable to the life tenant in excess of the non-recoverable interim payments, the obvious answer is that the interim payments are ordered made when earned; and the ascertainment of the fact of an adequate participation by income is not only unknown but also unknowable at the time the statute requires the interim payments to be made."

### **CONCLUSION.**

The order and decree appealed from, in so far as they apply the provisions of Subdivision "2" of Section 17-c Personal Property Law, should be reversed and said subdivision adjudged unconstitutional.

Respectfully submitted,

FRANCIS J. MAHONEY,  
*Counsel for Appellants.*

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# Supreme Court of the United States

OCTOBER TERM, 1943.

No. 52.

WILLIAM J. DEMOREST JR., ANN DEMOREST and CAROLYN  
DEMOREST by GERALD P. CULKIN, their Special Guardian,  
Appellants,

v.

CITY BANK FARMERS TRUST COMPANY, as Trustee under  
the Will of HENRY C. WEST, Deceased, et al.

---

## BRIEF FOR RESPONDENT EMMA M. WEST

---

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*Emma M. West.*

ALBERT B. MAGINNES,  
GEORGE D. MUMFORD,  
*of Counsel.*



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# Supreme Court of the United States

OCTOBER TERM, 1943.

No. 52.

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WILLIAM J. DEMOREST JR., ANN DEMOREST and CAROLYN  
DEMOREST by GERALD P. CULKIN, their Special Guardian,  
Appellants,

v.

CITY BANK FARMERS TRUST COMPANY, as Trustee under  
the Will of HENRY C. WEST, Deceased, et al.

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## BRIEF FOR RESPONDENT EMMA M. WEST

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### Reference to Official Reports of Opinions

The opinion of the Surrogate's Court is reported in 175 Misc. 1044. The majority opinion of the Court of Appeals is reported in 289 N. Y. 423.

The dissenting opinions of the Court of Appeals are reported in 289 N. Y. 432 *et seq.*

### Jurisdiction

The appeal is taken on behalf of infant remaindermen of a trust, by their Special Guardian, from an order of the Court of Appeals of the State of New York, dated January 15, 1943, and filed on remittitur in the office of the Clerk of the Surrogate's Court, County of New York, on January 25, 1943, which affirmed an order

of the Appellate Division of the New York Supreme Court, First Department, which had affirmed a decree of the Surrogate's Court, County of New York, judicially settling the intermediate account of proceedings of City Bank Farmers Trust Company, as Trustee under the will of Henry C. West, deceased, and directing, among other things, the distribution of the income received from certain parcels of real estate acquired by the accounting Trustee on foreclosure of mortgages, in accordance with the provisions of subdivision 2 of Section 17c of the Personal Property Law of the State of New York.

Emma M. West, the widow of testator, is respondent on this appeal and maintains the constitutionality of said statute.

### **Question Presented**

The appellants contend that this statute violates the Fourteenth Amendment of the Constitution of the United States of America "because it is retroactive and deprives appellants of property without due process of law and deprives appellants of rights guaranteed to them by said Fourteenth Amendment" (Appellant's brief, p. 2).

### **Statute Involved**

The statute involved in the appeal is Section 17-c of the New York Personal Property Law, being Chapter 452 of the Laws of New York of 1940, effective April 13, 1940, and is set forth in the appendix to this brief.

### **Statement of Case**

The testator, died on May 1, 1934. His will bearing date December 14, 1928 was admitted to probate by decree of the Surrogate's Court of the County of New York on May 28, 1934 (Record, p. 26).

By the fifth clause of the will, testator directed the Trustee to hold the residuary estate in trust, and

“to apply the net income from said estate to the use of my wife, Emma M. West, during the term of her natural life, or until she shall remarry”.

Other provisions of the will reflect the intention of the testator that the life beneficiary shall receive the entire net income. Such are the directions that no sinking fund shall be set aside from the income of the securities to amortize premiums on securities, and that all extraordinary dividends or distributions, other than stock dividends, whether paid in bonds, cash or otherwise, shall be treated as income (Record, pp. 90, 91).

The testator appointed City Bank Farmers Trust Company as Executor and Trustee of said will. By decree dated August 10, 1936 the Executor's accounts were settled, and it was directed to pay to itself as Trustee the balance of the funds in its hands.

At the time of his death the testator was the owner of nine mortgages, payment of which was guaranteed by Bond & Mortgage Guarantee Company, now in liquidation. These mortgages were in each instance secured upon parcels of real estate located in the City of New York. After testator's death the real estate upon which the mortgages were secured was acquired by the Trustee either at sale upon foreclosure, or by deed in lieu of foreclosure.

The decree entered in the Surrogate's Court on the Executor's accounting adjudged and decreed that each of the properties so received “and transferred by said Executor to itself as Trustee under said decedent's will, be held in a separate account by the Trustee”, and that the questions of apportionment of the proceeds received upon the ultimate sale of the properties and the rights of the parties interested should be reserved for a future account-



ing and taken into consideration by the Court "in determining the proper apportionment of the proceeds of sale of said properties".

The Trustee, in obedience to the direction in the decree, has accounted for each of the properties in a separate schedule of the present account—Schedules Cb to Cj, both inclusive (Record, pp. 47-72).

In the case of two of the parcels, salvage has been completed by the resale of the properties acquired at foreclosure.

The account of the administration of each of the properties comprising the nine investments has been so kept by the Trustee as to identify the income earned by each parcel in each fiscal year. The account allots to the life tenant, in accordance with the provisions of Section 17-c of the Personal Property Law, the net operating income from the properties up to 3% per annum of the principal amount of the mortgages, derived from the mortgaged properties in those years in which it was earned. Section 17-c of the Personal Property Law, which became effective on April 13, 1940, affects retroactively the disposal of the principal and income from these mortgage investments. In so far as it purports to direct the apportionment to the life beneficiary of the trust of 3% of the net income derived from these investments—thereby superseding the so-called Chapal-Otis rule (*Matter of Chapal*, 269 N. Y. 464; *Matter of Otis*, 276 N. Y. 101)—it is claimed, on behalf of appellants, that it deprives them of property and of vested rights without due process of law, and is therefore repugnant to the Fourteenth Amendment of the Constitution of the United States (Specification of assigned error intended to be urged—brief of Special Guardian, p. 6).

## ARGUMENT

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### POINT I

Article 2 of subdivision 17-c of the Personal Property Law of New York is a procedural and remedial statute which confirms to the life beneficiary of a trust the right to receive during salvage a fixed proportion of the net income from the operation of real estate acquired by the the trustee upon the foreclosure of a mortgage investment. It displaces *pro tanto*, the Chapal-Otis rule which authorized trustees to use such net income for the repayment of advances made from principal for the foreclosure costs, tax arrears, and other expenses incurred in the protection of the mortgage investment.

A salvage operation, as the term is used herein, occurs when a mortgage in default is foreclosed and title to the real estate is acquired by the trustee. The real estate thus acquired is substituted for the mortgage in the hands of the trustee, and takes on its character of personality.

*Matter of Otis*, 276 N. Y. 101, 111-12;

*Löckman v. Reilly*, 95 N. Y. 64, 71.

The Courts have taken judicial notice of the collapse in real estate values which, during the years following the panic in 1929, required and still requires trustees, upon foreclosure of mortgage investments, to "buy in" the real estate at foreclosure sale for lack of other bidders.

*Matter of Flint*, 240 App. Div. 217, 226; *affd.*  
266 N. Y. 607;

*Matter of West*, 175 Misc. 1044, 1049.

In thus protecting such investments, trustees have been forced to use funds from the principal of the estate to pay the costs of acquisition, overdue taxes and the like.

Under the Chapal-Otis rule, trustees have used the net rentals of the acquired real estate as the source of reimbursement of the trust fund for the advances so made from principal, in violation of the rights of the life tenant. The correction of this injustice is one of the remedial purposes accomplished by the enactment of this new statute.

The case at bar furnishes a typical example of the unfortunate consequences resulting to life beneficiaries from the application of this rule. The testator provided that his widow should receive the net income from his residuary estate. His intention that she should receive it unimpaired is shown by the directions that there should be no amortization of premium on investments, and also that all extraordinary dividends be paid to her without diminution (Record, pp. 90-91). Yet the widow has received no income from the real estate acquired upon foreclosure of the mortgages held by her trustee, during the six years of administration shown by the account, although all of the nine salvaged properties, with a single exception, have been productive of net rentals in one or more of those years.

The Chapal-Otis rule, which the Guardian mistakenly claims to be a rule of property, under which vested interests have been acquired by his wards, is an outgrowth of the rules of equitable apportionment first expressed in the decisions in *Meldon v. Devlin* (1898), 31 App. Div. 146, affirmed 167 N. Y. 573, and *Matter of Marshall* (1904), 43 Misc. 238, and later in *Furniss v. Cruikshank* (1921), 230 N. Y. 495, 508-510, to govern the apportionment between life tenant and remaindermen of the proceeds of liquidation of real estate acquired by a trustee on foreclosure of a mortgage. These allowed the life beneficiary of a trust to

participate in the division of the proceeds received by a fiduciary upon the liquidation of an investment in unproductive real estate. The inequity of a denial to the life beneficiary of any benefit from such an investment was remedied by allowing him a participation in the proceeds of sale proportionate to the normal income which he would have received prior to liquidation had the real estate been productive. In neither of these cases, however, did the question arise of disposal of the rentals derived from the operation of the acquired real estate during a salvage operation.

In *Matter of Chapel*, 269 N. Y. 464, the Court of Appeals was first confronted with the question of the disposal of net rentals received by a trustee during salvage. The Court held that the proceeds of sale, upon completion of the salvage operation, should be used first to pay the expenses of the sale and the foreclosure costs, and next to reimburse the capital account for any advances of capital for carrying charges not theretofore reimbursed out of income from the property. *Matter of Chapel* was decided in 1936, and was shortly followed by the decision in *Matter of Otis*, 276 N. Y. 101, holding, at page 115, that until the original capital had been fully restored, the trustee had only a discretionary right to distribute income from the salvaged property to the life beneficiary.

Following that decision, at least one of the Surrogates held, in *Matter of Brainerd*, 169 Misc. 640, 642, that payment of income to a life beneficiary from property still held in an uncompleted salvage operation, is never permissible until the advances for salvage purposes have been fully repaid; "thereafter such payments may be made in the discretion of the trustee". As a result, trustees fearing a surcharge of their accounts, hesitated to make any payment of surplus income to life beneficiaries.

The Court may take judicial notice of the fact that accumulations of net rentals in large amounts received from

the operation of salvaged properties, are held by New York fiduciaries awaiting distribution to income beneficiaries when the disputed questions involved in this appeal have been determined. Opinion of Foley J. *Matter of West*, 175 Misc. 1044, at page 1049.

The purpose of the statute is expressed in the note of the Executive Committee of the Surrogates Association of the State of New York, printed as part of the statute. It was adopted to simplify the complicated Chapal-Otis rule, and to provide a fair and equitable apportionment of the proceeds of a salvage investment, which would protect the interests both of income beneficiaries and remaindermen.

## POINT II

**No right is given to the remaindermen either by common law or by statute, to share in the income of a trust fund, their sole right being to receive the principal of the fund upon the termination of the trust.**

**Net income derived from trust investments, after payment of carrying charges attributable to income, belongs to the life beneficiary.**

**Not only are the remaindermen of a trust not entitled to have income applied to the repayment of advances made from principal; any such use of income is contrary to the public policy of the State of New York, because it violates the statute which prohibits accumulations of income except for the benefit of an infant, during minority.**

(a)

In the dissenting opinion of Lewis, J., cited by the Guardian, it is maintained that "there had vested in the income beneficiary and the remaindermen respectively

prior to the effective date of Section 17-c, subdivision 2, a proprietary interest in each of the properties acquired by the Trustee" (Record, p. 125).

With great deference to the learned Judge, we submit that under New York law, title to the trust assets is vested in the trustee. The beneficiaries have merely a right to enforce the performance of the trust in accordance with the provisions of the trust instrument.

Section 100 of the Real Property Law provides:

"Except as otherwise prescribed in this chapter, an express trust, valid as such in its creation, shall vest in the trustee the legal estate, subject only to the execution of the trust, and the beneficiary shall not take any legal estate or interest in the property, but may enforce the performance of the trust."

This section of the Real Property Law is extended to personalty by Section 11 of the Personal Property Law.

*Williams v. Thorn*, 70 N. Y. 270;

*Matter of Van Kleeck*, 95 Misc. 40, affirmed 177 App. Div. 917.

Thus the right of the life beneficiary is to receive, when collected by the trustee, the net income of the trust fund; the right of the remaindermen is to receive the corpus of the fund upon the termination of the trust by the death of the life tenant.

*Matter of Central Hanover Bank and Trust Co. [Mormand]*, 176 Misc. 183, affirmed 263 App. Div. 801, affirmed 288 N. Y. 608.

As the Court of Appeals held in the instant case, *Matter of West*, 289 N. Y. 423 at page 428:

"After the initiation of the salvage operation, as before, both the life tenant and the remaindermen could compel the trustee to administer the trust and

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to apportion to each his just share of the income and principal, but not that of any particular asset of the trust. (*Lockman v. Reilly*, 95 N. Y. 64, 71; *Bennett v. Garlock*, 79 N. Y. 302, 320.) (Emphasis supplied.)

## (b)

Not only have the remaindermen no right to the income from a trust investment, but diversion of income from a life beneficiary and its use to repay principal advances made to protect a trust investment and thereby, indirectly, to increase the principal of a trust fund, is offensive to the law of New York which prohibits the accumulation of income, except for the benefit of an infant during his minority.

This prohibition is contained in Section 16 of the Personal Property Law, Laws of 1897, Chapter 417, Section 4, which provides as follows:

“An accumulation of the income of personal property, directed by any instrument sufficient in law to pass such property is valid:

1. If directed to commence from the date of the instrument or the death of the person executing the same, and to be made for the benefit of one or more minors, then in being, or in being at such death, and to terminate at or before the expiration of such minority.

. . . . .

3. All other directions for the accumulation of the income of personal property are void.”

In *Hascall v. King*, 162 N. Y. 134, it was held that a direction in a will to use income to pay off mortgage obligations, thereby increasing the capital of the estate by decreasing the burden thereon, constituted an invalid accumulation.

See also *Thorn v. deBreteuil*, 179 N. Y. 64.

In *Matter of Rogers*, 22 App. Div. 428, affirmed 161 N. Y. 108, Cullen, C. J., writing for the Court, empha-

sized the strict line of demarcation between the respective rights of life beneficiary and remaindermen. He said at page 431:

"If from the will of the testator it is apparent that he intended that the life tenant should receive as income that which as a strict matter of law would be principal, undoubtedly that intent should govern, for the testator could give the life tenant the power to consume the whole principal. Such was the case of *The Matter of James* (146 N. Y. 78). But if the intent is in the opposite direction, that that which the law holds to be income shall be treated as principal and go to the remaindermen, it is in effect an accumulation and wholly void. Our laws forbid accumulation except for the benefit of infants in being during their minority. \* \* \*

But if a testator's intent is to make that principal which is income, in the case of a trust of the nature of the one before us, such intent is not in conformity with law, but in express contravention of it. Therefore, the right of the remaindermen in this fund must rest on the legal character which the law impresses on the fund, and not on any intent of the testator."

The Court added:

"Our laws forbid accumulation except for the benefit of infants in being during their minority. No principle of public policy declared by our statute law has been more firmly and rigidly upheld by the courts than this inhibition against accumulations."

In the Courts below the Guardian sought to maintain that his wards had a vested right in the continuation of the Chapal-Otis rule which protected it from legislative change.

Such an argument is answered in *Second Employers' Liability Cases*, 223 U. S. 1, in which, at page 50, this Court said:

"A person has no property, no vested interest, in any rule of the common law. That is only one of the

forms of municipal law, and is no more sacred than any other. Rights of property which have been created by the common law cannot be taken away without due process; but the law itself, as a rule of conduct, may be changed at the will \* \* \* of the legislature, unless prevented by constitutional limitations. Indeed, the great office of statutes is to remedy defects in the common law as they are developed, and to adapt it to the changes of time and circumstances.' *Munn v. Illinois*, 94 U. S. 113, 134; *Martin v. Pittsburg & Lake Erie R. R. Co.*, 203 U. S. 284 294; *The Lottawanna*, 21 Wall 558, 577; *Western Union Telegraph Co. v. Commercial Milling Co.*, 218 U. S. 406, 417."

In *New York Central R. R. Co. v. White*, 243 U. S. 188, this Court said (p. 198):

"No person has a vested interest in any rule of law entitling him to insist that it shall remain unchanged for his benefit." (Citing numerous cases.)

In *Cooley on Constitutional Limitations*, 8th Edition, the learned author said, at page 749:

"First, it would seem that a right cannot be considered a vested right, unless it is something more than such a mere expectation as may be based upon an anticipated continuance of the present general laws; it must have become a title, legal or equitable, to the present or future enjoyment of property, or to the present or future enforcement of a demand, or a legal exemption from a demand made by another. Acts of the legislature, as has been well said by Mr. Justice Woodbury, cannot be regarded as opposed to fundamental axioms of legislation, 'unless they impair rights which are vested; because most civil rights are derived from public laws; and if, before the rights become vested in particular individuals, the convenience of the State procures amendments or repeals of those laws, those individuals have no cause of complaint. The power that authorizes or proposes to give, may always revoke before an interest is perfected in the donee'."

### POINT III

The statute, as interpreted by the New York Court of Appeals, is "fair and reasonable and protects the interests of both income beneficiaries and remaindermen". By simplifying, according to its declared purpose, the rules of procedure in mortgage salvage operations, and laying the basis of apportionment, as between life beneficiaries and remaindermen of a trust, of the proceeds of salvage operations, it constitutes a valid enforcement of the economic policy of the State of New York.

The interpretation placed upon the statute by the highest New York court is conclusive upon the Federal Courts.

The fact that the statute operates retroactively to change the previously existing rule, by giving the life beneficiary of a trust the right to the payment of a reasonable share of the net income earned during the continuance of a salvage operation, and postponing repayment of principal advances until its final liquidation, does not deprive remaindermen of any property right without due process of law, within the meaning either of the Federal or State Constitutions.

(a)

The formula provided by Section 17-c merely gives the life beneficiary, in place of the right which he has always possessed, of requesting his trustee, in its discretion, to pay him the distributable income from the trust estate—the definite right to insist upon the limited exercise of that power by his trustee. In the words of the statute:

"The general rules of the apportionment of the proceeds of sale between life tenant and remaindermen are retained subject to the express modifications made herein."

The new statute removes the injustice which resulted from application of the Chapal-Otis rule authorizing the Trustee to apply the income of the life tenant first to the repayment of advances from principal. The life tenant will now receive the 3% of surplus income specified by the statute, without the obligation of recoupment, and only the excess may be used for the repayment of advances from principal. After repayment of these advances, the balance, if any, remaining is impounded to await ultimate apportionment of the proceeds of sale. The allotment to the life tenant of the initial 3% is to be taken into account and charged against the life tenant in the final apportionment of the proceeds of sale.

Appellants sought to maintain in the Courts below a fancied inequity, reiterated at pages 16-17 of the Guardian's brief, based on the contrast between a salvage operation settled by a decree made prior to the date of statutory enactment, April 13, 1940, and a salvage operation uncompleted by decree until after the date of the statute. In the case first assumed, it is asserted that the rights of principal and income would have been determined by the Chapal-Otis rule; in the second assumed case, the remaindermen would be relegated to the statutory formula for recognition of their rights. The answer is that unless the Chapal-Otis rule gives the remaindermen vested rights, they have no grievance resulting from its abrogation.

Moreover, the argument is based upon a misunderstanding of the law. The termination of the salvage operation is not effected by the entry of a decree upon the accounting of the fiduciary; it is effected by the resale by the fiduciary of the real estate acquired upon foreclosure. It was so held by the Surrogate in the case at bar—175 Misc. at page 1061, and on appeal by the life beneficiary from this part of the decree, the decision was upheld (Record, p. 122).

Elsewhere it is asserted that there might be validity to the statute if it provided first for an adjudication of the

intent of the testator, but that under the provisions of the statute there is a forced adjudication of such intent, which renders the statute unconstitutional (Guardian's brief, pp. 24-25).

This argument ignores the principle stated by Cullen, C. J., in *Matter of Rogers*, *supra*, quoted at page 11 of this brief, that the right of the remaindermen must rest on the legal character which the law impresses on the fund and not on any intent of the testator.

This statute does no more than to observe and enforce this distinction, and the argument is erroneous that the statute adjudicates the intent of a testator. No deprivation of due process results.

A further statement in Judge Lewis' dissenting opinion, which is the basis of the Guardian's argument at pages 10 to 12, must be challenged. It is suggested that Section 17-c, subdivision 2, accomplishes a mandatory transfer to the life tenant of property rights which had become vested in the remaindermen under a rule of property which antedated the enactment of the statute. It cannot well be argued that a rule of property was established by the Chapal-Otis rule, when the Court of Appeals has declared in interpretation of its own decision, in *Matter of Otis*, *supra*, at page 115:

"Perhaps it should be added that a general rule for such situations cannot be attained at a bound; that no rule can be final for all cases, and that any rule must in the end be shaped by considerations of business policy."

And it later declared in *Matter of West*, *supra*, at page 431:

"As already noted, the rules of administration heretofore set forth were tentatively stated and expressly recognized as subject to change. Before a judicial declaration, thus tentatively stated, becomes a rule of property, it must have become permanently fixed and long continued."



It is obvious that no vested rights can be founded upon any rule which is contrary to the public policy of the State.

In *Nebbia v. New York*, 291 U. S. 502, this Court said at page 537:

"So far as the requirement of due process is concerned, and in the absence of other constitutional restriction, a state is free to adopt whatever economic policy may reasonably be deemed to promote public welfare, and to enforce that policy by legislation adapted to its purpose. The courts are without authority either to declare such policy, or, when it is declared by the legislature, to override it. If the laws passed are seen to have a reasonable relation to a proper legislative purpose, and are neither arbitrary nor discriminatory, the requirements of due process are satisfied, and judicial determination to that effect renders a court *functus officio*."

In *Chicago, B. & Q. R. R. Co. v. McGuire*, 219 U. S. 549, at page 569, the Court said:

"The scope of judicial inquiry in deciding the question of *power* is not to be confused with the scope of legislative considerations in dealing with the matter of *policy*."

The Court cited the following statement from the opinion in *McLean v. Arkansas*, 211 U. S. 547, 548:

"The legislature, being familiar with local conditions is, primarily, the judge of the necessity of such enactments. The mere fact that a court may differ with the legislature in its views of public policy, or that judges may hold views inconsistent with the propriety of the legislation in question, affords no ground for judicial interference, unless the act in question is unmistakably and palpably in excess of legislative power." (Cases cited.)

## (b)

The interpretation of the statute by the New York Court of Appeals is binding upon the Federal Courts. It was held in *West v. A. T. & T. Co.*, 311 U. S. 223, 236, that the pronouncement of a State Court "is to be accepted by federal courts as defining state law".

As was said by Mr. Justice Brandeis in *Eric R. R. v. Tompkins*, 304 U. S. 64, 78:

"Except in matters governed by the Federal Constitution or by acts of Congress the law to be applied in any case is the law of the State. And whether the law of the State shall be declared by its Legislature in a statute or by its highest Court in a decision is not a matter of federal concern."

In *Morley v. Lake Shore Ry. Co.*, 146 U. S. 162, 166, 167, this Court said:

"The construction given to a statute of a state by the highest judicial tribunal of such state is regarded as a part of the statute, and is as binding upon the courts of the United States as the text. *Leffingwell v. Warren*, 2 Black 599, 603. The meaning of a state statute, declared by the highest court of a state, is conclusive upon this court. *Randall v. Brigham*, 7 Wall 523, 541. \* \* \* our only inquiry must be as to the validity of the statute itself, as construed by the State Court."

## (c)

There remains to be considered the question whether, as insisted by the Guardian, the retrospective operation of the statute renders it unconstitutional.

On this point the decision of this Court in *Kuehner v. Irving Trust Co.*, 209 U. S. 445 seems particularly apposite.

In that case subsection (b) of Section 77B of the Bankruptcy Act was attacked on such ground. The act limited

the claim of a lessor for indemnity under a covenant in a lease to a sum not exceeding the rent received under the lease for a three year period. The lessor had in 1926 leased certain real estate to its lessee for a term expiring in 1946. In 1932 the lessee was adjudicated a voluntary bankrupt. The Trustee in bankruptcy of the lessee rejected the lease and abandoned the premises. The lessor re-entered and terminated the leasehold in accordance with the provisions of the lease, which contained a covenant by the lessee to indemnify the lessor against all loss of rent from such termination. The Trustee thereupon relet the premises to a new lessee for a lesser rental. In 1934, immediately after Section 77 B had become a law, the bankrupt lessee filed a petition for reorganization under the new statute, which was approved by the Court. The claim of the lessor for damages measured by the difference between the rent reserved upon the reletting, and the rent reserved under the lease for the remainder of the term, was disallowed, except to the extent of an amount equal to the rental for three years. In certiorari proceedings the lessor claimed that it had been deprived of its property without due process of law. This Court rejected the contention, stating at page 452:

"While, therefore, the Fifth Amendment forbids the destruction of a contract, it does not prohibit bankruptcy legislation affecting the creditors' remedy for its enforcement against the debtors' assets or the measure of the creditor's participation therein, if the statutory provisions are consonant with a fair, reasonable and equitable distribution of those assets. . . . The question is whether the remedy is circumscribed in so unreasonable and arbitrary a way as to deny due process."

And later in its opinion, the Court, commenting upon its decision in *City Bank Farmers Trust Co. v. Irving Trust Co.*, 299 U. S. 433, said:

"In framing the reorganization statute Congress obviously attempted to award landlords an equitable

share in the debtor's assets as in justice it was bound to do, since the purpose was to discharge the debtor from liability to future suits based upon the lease. It is incorrect to say that Congress took away all remedy under the lease. On the contrary, it gave a new and more certain remedy for a limited amount in lieu of an old remedy inefficient and uncertain in its result. This is certainly not the taking of the landlord's property without due process."

In *People ex rel. Eitel v. Lindheimer*, 371 Ill. 367, 21 N. E. (2) 318—appeal dismissed 308 U. S. 505—the Supreme Court of Illinois held that appellees had no vested rights under a statute which gave them an action to recover excess taxes paid through mistake or overassessment, and that a subsequent repealing statute, even though it was enacted after the commencement of an action under the old statute, and operated retrospectively to terminate appellees' right to proceed under the old statute, was not unconstitutional. Answering the argument of unconstitutionality, the Illinois Court said at page 321:

"A retrospective statute affecting vested rights is very generally considered in this country as founded on unconstitutional principles and consequently inoperative and void; but this doctrine is not understood to apply to remedial statutes of a retrospective nature not impairing contracts or disturbing absolute vested rights. . . ."

Appellees argue that the repealing statute is of doubtful constitutionality, but since we have held that no vested rights are involved, it is not necessary to consider that question."

The constitutionality of Section 480 of the New York Civil Practice Act, which provided that interest should be added to recoveries in actions for unliquidated damages caused by breach of contract was under review in *J. P. Preston Co. v. Funkhauser*, 261 N. Y. 140; 290 U. S. 163.

The Court held that the provision for the enlarged remedy was consistent with the substantial rights of the parties under their contract, and could not be regarded as an unreasonable exercise of legislative power.

It is to be noted that in most of the foregoing cases, a contract right was involved—a circumstance absent from the case at bar in which no contract or other rights are involved than those claimed to be vested in appellants by an alleged rule of law which they seek to apply to the provisions of a testamentary trust.

Many other decisions may be cited in which statutes affecting remedies or procedure have been upheld by the Appellate Courts of New York as constitutional, notwithstanding their retroactive operation.

*Matter of City of New York*, 290 N. Y. 236, where the Court of Appeals upheld the constitutionality of Chapter 668 of the Laws of 1941 which provided an additional method to enforce payment of tax liens, to operate retroactively. At page 241 of the opinion, the Court said:

“Stress is laid by the appellant-taxpayer on the retroactive effect of the statute. As to this, we think it sufficient to observe that a new remedy for the collection of taxes may validly be made applicable to taxes theretofore delinquent. (See *League v. Texas*, 184 U. S. 156; *Phillips v. Commissioner of Internal Revenue*, 283 U. S. 589, 601; *Matter of Trustees of N. Y. P. E. Public School*, 31 N. Y. 574, 584, 585; *City of New York v. Appleby*, 219 N. Y. 76.)”

*Brearley School v. Ward*, 201 N. Y. 358, holding that an execution under Section 1931 of the Code of Civil Procedure as amended by Chapter 148 of the Laws of 1908, could lawfully be issued against the income of a trust fund, although the trust was created prior to the passage of said Act, which removed the prior exemption of such income from execution.

*Laird v. Carton*, 196 N. Y. 169, involving Chapter 148 of the Laws of 1908, which extended the scope of an execution which could be issued upon a judgment, to recover wages, earnings or salary of the judgment debtor;

*Matter of Berkovitz v. Arbib & Houlberg*, 230 N. Y. 261, making the Arbitration Law, Chapter 275 of the Laws of 1920, applicable to pre-existing contracts;

*Matter of Barker*, 230 N. Y. 364; *Robertson v. Brulatour*, 188 N. Y. 301, and *Matter of Rotter*, 106 Misc. 113, 115, in which cases the validity was challenged of statutes which increased the commissions allowed to trustees on judicial settlements of their accounts and applied the new rates to trusts existing before the enactment of the statute.

Instances may be conjectured, as in the opinion in *Matter of Wacht*, 32 N. Y. Supp. 2d, 871, by which a life beneficiary might conceivably receive, under the rule declared by the statute, more than the share allocable to him out of the proceeds of a salvage operation, according to the Chapal-Otis rule. The situations used as illustrations by the learned Surrogate to establish his point have not yet arisen in practice. Until they do, they furnish no basis for an attack on the constitutionality of this law.

## CONCLUSION

**The decision of the Court of Appeals for the Second Circuit is correct and should be affirmed.**

Respectfully submitted,

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Emma M. West.

ALBERT B. MAGINNES,  
GEORGE D. MUMFORD,  
of Counsel.



## Appendix

§ 17-c. Real property acquired by foreclosure or conveyance in lieu thereof.

1. Unless otherwise expressly provided in a will, deed of trust or other instrument, in any case in which an executor or a trustee under a will or deed of trust or other instrument shall hold a mortgage upon real property for the benefit of one or more tenants for life or limited term, with remainder over, and such executor or trustee shall acquire title to such real property by foreclosure or conveyance in lieu of foreclosure, such acquired real property shall be and become a principal asset in lieu of such mortgage. Such tenant or tenants for life or limited term shall be entitled to the net income from such acquired real property from the date of its acquisition.

After the date of the taking effect of this section, no allocation or apportionment as between life tenant and remainderman, of the proceeds of the sale of the real property previously subject to a mortgage shall be made. The rules of procedure now or heretofore applicable to such allocations or apportionments of the proceeds of sale are hereby abolished.

The expenses of foreclosure or of conveyance in lieu of foreclosure and the arrears of taxes and other liens which accrued prior to such foreclosure or conveyance shall be charges payable out of principal. Where any moneys have been advanced out of income to pay such expenses, taxes or other liens, they shall be reimbursed to income out of principal.

The terms and rules of procedure of this subdivision shall apply only to the estates of persons dying after its enactment and to trusts created under a deed of trust or other instrument executed after its enactment and to in-

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vestments of mortgages hereafter made by a trustee of an existing trust, whether testamentary or inter vivos.

2. The existing rules of procedure applying to salvage operations respecting existing mortgage investments are continued except as modified by the subparagraphs hereinafter set forth. The terms and rules of procedure of this subdivision shall apply specifically (a) to the estates of persons dying before its enactment and (b) to mortgages on real property held by a trustee under a deed of trust or other instrument executed before the date of its enactment and (c) to real property acquired by foreclosure of mortgage or real property acquired in lieu of foreclosure before or after the date of its enactment in trusts created or mortgage investments made prior thereto, and (d) to any pending proceeding or action for an accounting of the transactions of an executor or trustee.

(a) Net income during the salvage operation up to three per centum per annum upon the principal amount of the mortgage shall be paid to the life tenant, regardless of principal advances for the expenses of foreclosure or of conveyance in lieu of foreclosure and arrears of taxes and other liens which occurred prior to such foreclosure or conveyance and the cost of all capital improvements. Any payment of net income heretofore or hereafter made to the life tenant up to such three per centum per annum shall be final and shall be not subject to recoupment from the life tenant or as a surcharge against the trustee or executor. The amount of all such payments shall be taken into account, however, in the apportionment of the proceeds of sale and shall be charged against the share of the life tenant.

(b) The foregoing principal advances shall be repaid out of excess net income above such three per centum per annum. When principal advances have been satisfied, any

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excess income shall be impounded (subject to reinvestment under the terms of the will or deed) to await sale and apportionment.

(c) The unpaid principal advances shall be a primary lien upon the proceeds of sale and shall be paid first out of any cash so derived. If insufficient the balance shall be a primary lien upon any purchase money mortgage received upon the sale.

(d) The purpose of the enactment of this subdivision is declared to be the simplification of the rules of procedure in mortgage salvage operations and the elimination of present complications which work to the disadvantage of the life tenant, who is usually the principal object of the testator's or settlor's bounty, by depriving him of a fixed right to the actual payment of any net income earned by the property. Such fixed right is granted in lieu of the discretion now given to the trustee to pay net income or any part thereof to the life tenant. The general rules of the apportionment of the proceeds of sale between life tenant and remainderman are retained subject to the express modifications made herein. Only equitable adjustments and balances as between the parties are intended to be effectuated by the provisions of this subdivision. If any provision of this subdivision or the application thereof to any mortgage or acquired property by foreclosure or conveyance, or to any trust is held invalid, the remainder of the subdivision and the application of such provision to any other mortgage or property acquired by foreclosure or conveyance or other trust shall not be affected thereby.

3. The term "mortgage" as used herein shall include a mortgage participation or a mortgage certificate or any other form of interest in a whole mortgage but shall not

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include a mortgage participation or a mortgage certificate or any other form of interest in a group of mortgages.

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Note of Commission.—“This bill is proposed by the executive committee of the Surrogates’ Association of the State of New York. Its general purposes are:

“(1) To simplify the complicated rules restated in *Matter of Chapal* (269 N. Y. 464) and in *Matter of Otis* (276 N. Y. 101) relating to mortgage salvage operations (a) in existing trusts as to mortgages hereafter acquired as a trust investment and (b) in testamentary trusts created by the will of decedent dying after its enactment and (c) in inter vivos trusts created by an instrument executed after its enactment. Such simplification is provided in the first subdivision of the new section.

“It has been the policy of the legislature to simplify the administration of estates of decedents and to save expense to the beneficiaries. In recent years section 17-a of the Personal Property law was enacted to avoid the difficult problems of the allocation of stock dividends received during the period of a trust. Under that section they are now allocated wholly to capital. Section 17-b of the Personal Property law was enacted to abolish the intricate rule in *Matter of Benson* (96 N. Y. 499) under which it was necessary to capitalize the income on monies held within the estate for the payment of administration expenses, debts, taxes and pecuniary legacies. In line with this policy the proposed legislation contained in the first subdivision abolishes, in the instances stated above, the Chapal-Otis rules, and will substitute a simple form of the treatment of the foreclosed real property as a principal asset of the trust. It is to be treated just as a railroad bond upon which default in interest before sale has occurred.

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“(2) Further modifications are proposed by the second subdivision of the section as to mortgage investments already made in existing trusts. The present rules for apportionment between life tenant and remainderman under the Chapal-Otis cases are continued as to existing trusts where the investment in a mortgage has been made, with modification thereof in two specific instances.

“(a) The Chapal-Otis rule authorizes the trustee to pay surplus net income in his discretion. Trustees have hesitated to pay such net income because in the case of overpayment to the life tenant, the trustee might be surcharged with that amount. The life tenant of the trust must wait in the majority of cases for a long period of time before he becomes entitled to the payment of any income, because of the present requirement that advances from principal for the expenses of foreclosure and for arrears of taxes and other liens must first be paid from the net income of the property. The amendment provides for the immediate payment of income to the life tenant beginning with the date of the acquisition of the property by the trustee by foreclosure or conveyance in lieu of foreclosure. Under the new provisions net income up to three per centum of the face amount of the mortgage is so payable. Under the Chapal-Otis rules the life tenant is entitled in the final apportionment to the inclusion of interest at the mortgage rate during the period of the salvage operation. The rate of three per centum in the new section has been recommended as a fair return to the life tenant and at the same time a protection to the remainderman in the event that the property is sold at less than the face amounts of the income and principal shares employed as the ratio of the apportionment. (b) Surplus net income above three per centum is to be applied to the payment of advances from principal until the amount of such advances are satisfied. When the property in the

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salvage operation is sold, the unpaid balance of principal advances must be satisfied first out of the cash received from the sale. If there be any unpaid balance due for principal advances, it is made a primary lien upon the purchase money mortgage. The amendment further directs that after principal advances have been paid, the surplus net income above three per centum, accruing during the salvage operation, shall be held by the trustee to await sale and apportionment under the Chapal-Otis rules."



DEC 3 1943

# Supreme Court of the United States

OCTOBER TERM, 1943

No. 52

WILLIAM J. DEMOREST, JR., ANN DEMOREST and CAROLYN  
DEMOREST by GERALD P. CULKIN, THEIR SPECIAL  
GUARDIAN,

*Appellants,*

*against*

CITY BANK FARMERS TRUST COMPANY, as Trustee under the  
will of Henry C. West, Deceased, *et al.*,

*Respondent.*

## BRIEF FOR RESPONDENT TRUSTEE

C. ALEXANDER CAPRON,  
*Counsel for Respondent Trustee.*

J. KARR TAYLOR,  
J. DINSMORE ADAMS,  
*Of Counsel.*

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# Supreme Court of the United States

OCTOBER TERM, 1943

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No. 52

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WILLIAM J. DEMOREST, JR., ANN DEMOREST and CAROLYN  
DEMOREST by GERALD P. CULKIN, THEIR SPECIAL  
GUARDIAN,

*Appellants,*

*against*

CITY BANK FARMERS TRUST COMPANY, as Trustee under the  
will of Henry C. West, Deceased, *et al.*,

*Respondent.*

---

## **BRIEF FOR RESPONDENT TRUSTEE**

### **Opinions Below**

The opinion of the Court of Appeals (R. 117) is reported in 289 N. Y. 426 and the dissenting opinions (R. 122 and 128) are reported in 289 N. Y. 432, 437.

The opinion of Surrogate FOLEY in the Surrogate's Court of New York County (R. 93) is reported in 175 Misc. 1044.

The Appellate Division of the Supreme Court affirmed the Surrogate's decree without opinion (R. 114), 264 App. Div. 701.

### **Jurisdiction**

The jurisdiction of this court rests on Section 237(a) of the Judicial Code as amended by the Act of February



13, 1925, Chapter 229, 43 Stat. 936 [28 U. S. C. A. Sect. 344(a)], which confers jurisdiction on this court to review a final judgment or decree, in any suit in the highest court of a State, where there is drawn in question the validity of a statute of such State on the ground of its being repugnant to the Constitution of the United States, and the decision is in favor of its validity. The right of review on appeal, instead of a writ of error, was conferred by the Act of January 31, 1928, Chapter 14, Section 1, 45 Stat. 54 and the Act of April 26, 1928, Chapter 440, 45 Stat. 466 [28 U. S. C. A. Sect. 861a, 861b].

### **Question Presented**

The question presented is whether Subdivision 2 of Section 17(c) of the Personal Property Law of New York deprives the appellants of property without due process of law, and, therefore, violates the Fourteenth Amendment of the Constitution.

The statute establishes rules of administration with respect to real property acquired by a trustee on the foreclosure of a mortgage. The only portion of the statute, which is claimed to violate constitutional limitations, is that which directs the trustee to treat as income and pay to the life beneficiary a limited portion of the net rents of each property acquired on the foreclosure of a mortgage, not to exceed in any year an amount equal to 3% of the principal of the foreclosed mortgage.

It is asserted that the statute attempts to change a rule theretofore established by the courts of New York, pursuant to which the rents, so required to be paid to the life beneficiary, would constitute capital of the trust to which the remaindermen will be entitled on the termination of the life estate; that, in effect, the statute takes the property of the remaindermen and gives it to the life beneficiary, and, therefore, the remaindermen are deprived of property without due process of law.

It has also been asserted that the legislature could not prescribe regulations for the administration of such fore-

closed properties, because this was within the exclusive jurisdiction of the courts.

## **Statement**

### **Concerning the Proceeding**

This proceeding was instituted, in the Surrogate's Court of the County of New York, by the respondent trustee, which applied for the judicial settlement of its account and for instructions concerning the distribution of rents and the proceeds of sale of real properties acquired by the trustee on the foreclosure of mortgages. In some instances, deeds in lieu of foreclosure were accepted, but as this is without significance on the question presented, in this brief we have treated all such properties as having been acquired on foreclosure.

The trustee's account conformed to the requirements of the statute and credited to income that portion of the rents from such properties which the statute directed should be paid to the life beneficiary. The account, with minor adjustments not here important, was allowed and settled and instructions were given to the trustee to effect distribution of the net rents as required by the statute. The Appellate Division of the Supreme Court and the Court of Appeals affirmed the Surrogate's decree in all respects. The remaindermen of the trust through their special guardian have now appealed from the judgment of affirmance of the Court of Appeals.

### **Concerning the Estate**

Henry C. West died in 1934. He left no issue and his widow was the chief object of his bounty. By his will (R. 90) he gave her a legacy of \$25,000 and the income from his residuary estate during her widowhood, less \$100 per month during her life, which he bequeathed to his brother. After the termination of the trust for his widow, he gave the income from \$30,000 to a nephew for life and the balance of his residuary estate to a niece or her issue and to issue of

his wife's niece. His desire to provide adequately for his widow is further emphasized by the direction that income was not to be diminished by setting up a sinking fund to amortize the premiums on securities, and that extraordinary dividends, other than stock dividends, should be deemed income; also by the authority granted to his trustee to retain investments made by him and to make new investments not limited to those classes, in which trustees are authorized by law to invest (R. 92).

At the time of his death his residuary estate amounted to approximately \$147,000 if his bonds and mortgages are valued at par.\*

The residuary estate consisted chiefly of bonds and mortgages owned by the testator. At the date of the account (July 31, 1940, R. 41), except for approximately \$10,000 in bonds, the capital of the trust consisted wholly of bonds and mortgages and real properties acquired by the trustee on the foreclosure of other mortgages.

During the course of the administration of the estate, nine mortgages, securing in the aggregate \$44,000 of principal, were foreclosed because of defaults in the payment of interest. In addition to the loss of interest on those bonds and mortgages, the income of the trust was further reduced by the income from \$19,000 of capital which was used to pay the capital charges involved in connection with such foreclosures, including back taxes and the cost of rehabilitating the properties, operating expenses, etc. The following schedule shows this in greater detail:

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\* This amount is arrived at by adding to the item of \$133,104.64 (R. 40) the difference between the par and the appraised value of certain bonds and mortgages, to wit, \$5,162.50; also, the sums expended by the executors before the properties were transferred to the trustees in connection with foreclosed mortgages, to wit, \$8,785.39, the last two amounts being the aggregates computed from numerous items set forth in the account.

Premises	Principal of Mortgage	Principal Advances	Date From Which Int. Was Due	Reference Record, Pages
46 North St., Brooklyn .....	\$ 4,000.	\$ 3,494.98	11/1/33	47, 50
1855 E. 7th St., Brooklyn .....	7,000.	2,770.74	6/1/32	50, 53
2082 E. 9th St., Brooklyn .....	7,000.	4,242.66	4/1/34	53, 56
193 Bay 17th St., Brooklyn .....	5,000.	1,563.87	5/1/34	56, 59
1441-3 66th St., Brooklyn .....	4,500.	1,205.52	12/1/34	59, 62
2047 E. 27th St., Brooklyn .....	4,250.	2,028.54	11/1/32	62, 65
240 Floyd St., Brooklyn .....	3,000.	1,247.88	7/1/35	65, 68
168 Morrison Ave., New Brighton, Staten Island .....	4,500.	975.95	6/1/34	68, 69, 70
41 Montrose Ave., Brooklyn .....	4,750.	1,582.77	7/1/35	70, 72
	<u>\$44,000.</u>	<u>\$19,112.91</u>		

Of these nine properties only two had been sold prior to the date of the account. The parcel, 168 Morrison Avenue, was sold on August 25, 1939, for \$4500 in cash (R. 19). The parcel, 41 Montrose Avenue, was sold on August 9, 1939, for \$4000 of which \$800 was paid in cash and the balance by a purchase money mortgage. The aggregate of the net rents from this property, plus the cash proceeds of sale, were not sufficient to pay off the principal advances made in connection with this parcel.

As a result of the foregoing, the widow was deprived for a substantial period of income from some \$63,000 of capital, or 43% of the trust established for her benefit, except for such rents as might be payable to her and such deferred income as she may be entitled to receive on the sale of such properties and the collection of any purchase money mortgages which are accepted as partial payments for such properties.

**Concerning the Rules of Administration Promulgated by  
the Courts With Respect to Such Properties.**

When Henry C. West made his will in 1928 and when he died in 1934, he had no reason to fear that, if any of his mortgages were foreclosed, his widow could not use as income the rents from real property thereby acquired. At that time no decision had been rendered by any New York court suggesting that rent from real property would not be accorded its traditional character and treated as income, if such real property were acquired by a trustee upon the foreclosure of a mortgage. The only case, in which the matter of surplus rents was in any way involved, recognized that these should be credited to income (*Van Fleck v. Lounsbery*, 34 Hun 565; Gen. Term, N. Y. Sup. Ct.; 1885). There the court rejected a claim that profits should be credited to income on the ground that interest on the mortgage and rents after foreclosure had been credited to income.

At an early date, the equitable rule was developed that, if property acquired by a trustee on the foreclosure of a mortgage was not productive of income during the period it was held by the trustee, then upon the sale thereof recognition should be given to the loss of income suffered by the life beneficiary and, therefore, that the proceeds of sale should be ratably apportioned between principal and income. However, there was conflict in the authorities as to the basis on which such apportionment should be made. In *Roosevelt v. Roosevelt*, 5 Redf. 264 (N. Y. Surr. Ct., 1881), the apportionment was made by finding the sum, which, with interest from the testator's death (the judgment of foreclosure having been rendered prior to his death) to the date of sale of the premises, would equal the net proceeds of sale. That amount was credited to capital and the balance to income. The interest was there computed at the equitable rate, that is the rate at which funds might have been prudently invested. In *Meldon v. Dertin*, 31 App. Div., 146, 158 (1898), affirmed 167 N. Y. 573, the court approved a judgment directing that the proceeds of sale



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should be apportioned between the principal and income of the trust "in the ratio which the aggregate principal of the mortgage bears to the whole unpaid interest." No reference was made in either case to the disposition of rents. Apparently none was received by the trustees.

The rule with respect to apportionment was further amplified by a full and well-considered opinion in *Matter of Marshall*, 43 Misc. 238 (Westchester Co. Surr. Ct., 1904). In that case, also, no rents were produced as the property was unimproved. Substantial carrying charges were incurred which were paid out of the capital of the trust. The Surrogate stated that the amount of principal invested in the property upon which the apportionment should be based included, not only the principal of the mortgage, but all sums advanced out of capital in connection with the property, and that the income invested in the property should be deemed to be the interest "upon the principal locked up in the property, that is the original amount of the mortgage and the various amounts of principal paid out for taxes, assessments, etc., from time to time" (pp. 240-241). The Surrogate further held that, for the purpose of determining the amount of income invested in the property, interest should be computed not at the rate specified in the mortgage but at the equitable rate (p. 246).

When the values of New York real estate collapsed in 1932, following the earlier decline in the securities market, it became necessary for many trustees to foreclose mortgages and to take over the underlying properties. The question, as to the rules of administration to be pursued by trustees with respect to such properties, then assumed importance. The subject was twice considered by the New York Court of Appeals, first in the *Matter of Chapal*, 269 N. Y. 464 (1936), and shortly thereafter in the *Matter of Otis*, 276 N. Y. 101; 277 N. Y. 650 (1937). In the latter case, the court stated that the rules expressed should not be regarded as final for all cases.

The rules stated have since come to be known as the *Chapal-Otis* rules. We summarize them. A separate ac-



count should be kept with respect to each property bought in on the foreclosure of a mortgage. All expenses in connection therewith should be temporarily advanced out of the capital of the trust, including all expenses of the foreclosure, back taxes, and carrying charges in excess of rents after the property is acquired by the trustee. All sums so advanced by capital are to be regarded as a first lien or charge on the property. Upon the sale of the property, the proceeds should be distributed as follows: All capital advances, remaining unpaid, should be restored first. The balance, plus any net rents not theretofore applied to the repayment of capital advances, should be apportioned between principal and income in the ratio in which each is deemed to be invested in the property. The principal of the mortgage is the amount of principal deemed to be so invested; the interest in default, and which would have been earned had the mortgage not been foreclosed, should represent income. From the amount apportioned to income, the net rents, if any, paid to the life beneficiary, as income, are to be deducted. If, upon the sale of such property, the trustee accepts a purchase money mortgage in partial payment, then the cash, remaining after payment of capital advances; and the purchase money mortgage should each be apportioned between principal and income in the ratio in which the total proceeds of the salvage operation are to be apportioned.

In addition to the foregoing, for the first time, the court discussed the disposition of the rents received from a property so acquired by a trustee. The court apparently thought that the rule of apportionment rested on the theory the mortgage is security both for principal and interest and that, when a trustee forecloses such a mortgage, he is engaging in a salvage operation for both. It concluded that the whole salvage operation, from the foreclosure to the final liquidation, should be treated as a single transaction and that the amount to be apportioned between principal and income is the aggregate of all sums received during the salvage operation, *i. e.*, the net rents plus the net proceeds of sale.

In *Matter of Chapal*, the court merely noted the direction in the Surrogate's decree that, if there should occur a deficiency of income to pay carrying charges, subsequent surplus rents should first be used to restore to capital such earlier deficiencies, but that, with respect to other surplus rents, trustees should "exercise their own discretion and judgment with respect to distributing such surplus income entirely or of retaining the same or some part thereof to meet possible subsequent deficiencies" (470-471). Later, in *Matter of Otis*, there were expressions which led some to believe that the court would not approve of the distribution of any rents to the life beneficiary until all capital advances, including expenses of foreclosure, back taxes, rehabilitation costs, as well as earlier carrying charges, had been fully restored.

In the case now before this court, the Court of Appeals said that, under its earlier decisions, a trustee did have the right to exercise discretion with respect to the distribution of any surplus rents. However, in its earlier decisions, the court gave no indication as to whether a trustee would incur liability, if, in the exercise of that discretion, it should distribute surplus rents to a life beneficiary and subsequently, on the completion of the salvage operation, it was found that the rents so distributed were in excess of the life beneficiary's share of the aggregate of the surplus rents and proceeds of sale. One of the surrogates stated that a trustee would be liable to surcharge for any such overpayment to a life beneficiary. *Matter of Brainerd*, 169 Misc. 640, 645 (Kings Co. Surr. Ct., 1938). The possibility of a distribution of rents resulting in such an overpayment existed in every case. None could say how much would be realized on a sale, or whether this would be sufficient to repay the capital advances. In view of this, many trustees deemed it improper for them to effect a distribution of any rents until all capital advances had been restored. In effect, this resulted in a denial of any payment to the life beneficiary until the sale of the property, for the capital advances were in most instances so considerable

they could not be repaid out of rents for a long period of years.

The situation of the widow, in the case now before the court, well illustrates the plight in which life beneficiaries were placed. Forty-three per cent of the capital of her trust was tied up in such properties. Most were throwing off surplus rents, but, if it were the duty of the trustee to use these to repay all capital advances, no rent could be paid to the widow for many years. In all probability, nothing could be paid to her prior to the sale of the respective parcels.

This situation was not limited to a few isolated instances. It existed throughout the State. For many years, bonds and mortgages had been a preferred investment for trust funds.

Thus, a grave question of public importance was presented—should trustees continue to accumulate rents from real property for the benefit of future generations and contrary to the public policy of the state against accumulations of income, or should they be used presently for the benefit of the life beneficiaries of such trusts?

It was at this juncture that the Legislature acted.

The legislation enacted was recommended by the Executive Committee of the Surrogates' Association of the State of New York, which committee was composed of a number of distinguished surrogates. To the draft legislation presented by this committee was appended the Committee's note explaining its purpose. With respect to subdivision 42) of the proposed statute, that portion which is here involved, the committee stated (Pocket Supplement, 40 McKinney's Consolidated Laws of New York, Section 17-c of the Personal Property Law):

... \* \*

(2) Further modifications are proposed by the second subdivision of the section as to mortgage investments already made in existing trusts. The present rules for apportionment between life tenant and remainderman under the Chapal-Otis cases are continued

as to existing trusts where the investment in a mortgage has been made, with modification thereof in two specific instances.

(a) The Chapal-Otis<sup>7</sup> rule authorizes the trustee to pay surplus net income in his discretion. Trustees have hesitated to pay such net income because in the case of overpayment to the life tenant, the trustee might be surcharged with that amount. The life tenant of the trust must wait in the majority of cases for a long period of time before he becomes entitled to the payment of any income, because of the present requirement that advances from principal for the expenses of foreclosure and for arrears of taxes and other liens must first be paid from the net income of the property. The amendment provides for the immediate payment of income to the life tenant beginning with the date of the acquisition of the property by the trustee by foreclosure or conveyance in lieu of foreclosure. Under the new provisions net income up to three per centum of the face amount of the mortgage is so payable. Under the Chapal-Otis rules the life tenant is entitled in the final apportionment to the inclusion of interest at the mortgage rate during the period of the salvage operation. The rate of three per centum in the new section has been recommended as a fair return to the life tenant and at the same time a protection to the remainderman in the event that the property is sold at less than the face amounts of the income and principal shares employed as the ratio of the apportionment. (b) Surplus net income above three per centum is to be applied to the payment of advances from principal until the amount of such advances are satisfied. When the property in the salvage operation is sold, the unpaid balance of principal advances must be satisfied first out of the cash received from the sale. If there be any unpaid balance due for principal advances, it is made a primary lien upon the purchase money mortgage. The amendment further directs that after principal advances have been paid, the surplus net income above three per centum, accruing during the salvage operation, shall be held by the trustee to await sale and apportionment under the Chapal-Otis rules."

The statute so recommended was adopted by the legislature.

### **The Statute**

The statute involved is subdivision (2) of Section 17-c of the Personal Property Law of New York, which was enacted by Chapter 452 of the Laws of 1940, in effect April 13, 1940. It is printed in full in the appellants' brief, pages 3 to 5.

### **Summary of Argument**

1. The statute deprives neither the life beneficiaries nor remaindermen of any property.

(a) The property rights of a beneficiary in a trust consist solely of the right to enforce its execution. They have no title to any of the assets of the trust, the same being vested in the trustee.

(b) For the most part, the testator left to the rules of administration the ascertainment of the net income and principal of the trust, the distribution of which he directed. The beneficiaries will receive all to which they are respectively entitled upon payment to the income beneficiary of the net income determined by the application of such rules and the distribution to the remaindermen of the principal similarly so determined.

(c) The *Chapal-Otis* rules were mere rules of administrative procedure. They were tentative, not final. They are not founded on established equitable doctrines, but were formulated as practical guides, based on considerations of business policy. Those parts with which we are here concerned were not in existence, either at the time the testator made his will or when he died, nor did they constitute a restatement of previously expressed principles or rules. The testator could not therefore be deemed to have adopted and embodied them in his will, so that a change in such rules would

defeat the disposition of his property, which he intended to make by his will.

(d) The beneficiaries of a trust have no vested right in the maintenance of any rule of administrative procedure with respect thereto.

(e) The statute did not reduce the amount which might have been paid either to the remaindermen or life beneficiaries of trusts under the *Chapal-Otis* rules.

2. It is a recognized principle of New York law that the legislature may make and modify rules of administrative procedure affecting trusts. Since the legislature had power to enact the remedial statute in question, and it is in all respects reasonable, and deprived none of any property, it did not exceed any limitations imposed by the Fourteenth Amendment to the Constitution.

## ARGUMENT

### I

**The statute deprives neither the life beneficiaries nor remaindermen of any property.**

#### (a)

The beneficiaries of a trust have no title to or interest in any particular asset of the trust, but solely the right to enforce the execution of the trust (*Bennett v. Garlock*, 79 N. Y. 302, 320; *City of Mt. Vernon v. County Trust Co.*, 199 N. Y. Supp. 500, not officially reported).

In respect of a trust of personal property, title to all the trust assets is vested solely in the trustee (*Matter of Wilkin*, 183 N. Y. 104, 110). No title or interest vests in the beneficiaries (*Knox v. Jones*, 47 N. Y. 389, 396). This doctrine applies specifically to mortgages, and to real property bought in by a trustee upon foreclosure of a mortgage (*Lockman v. Reilly*, 95 N. Y. 64).



## (b)

For the most part, the testator left to the rules of administration the ascertainment of the net income and principal of the trust, distribution of which he directed.

The beneficiaries will receive all to which they are respectively entitled, upon payment to the income beneficiary of the net income determined by the application of such rules, and the distribution to the remainderman of the principal similarly so determined.

The testator merely directed the trustee to pay and distribute the "net income" and the "principal" of the trust, not of any particular asset of the trust. He gave no direction with respect to his bonds and mortgages, nor with respect to the foreclosure of mortgages or the real property which might be acquired as a result thereof, nor with respect to the rents therefrom. He gave three specific directions bearing upon the determination of what should be deemed income or principal; (1) that no sinking fund should be set aside out of income to amortize the premiums on securities, (2) that stock dividends should be deemed principal, and (3) that all other extraordinary dividends should be treated as income. Aside from the foregoing, he gave the trustee no guide for the classification of receipts, nor whether particular expenses should be charged to principal or income. In the absence of further definition, the determination of net income and principal of the trust was subject to the application of rules of administration promulgated by the courts or by the legislature. As we shall show hereafter, both have heretofore participated in the formulation of rules of administration with respect to trusts.

## (c)

The *Chapal-Otis* rules were mere rules of administrative procedure. They were tentative, not final. They were not founded on established equitable doctrines, but were formulated as practical guides based on considerations of business policy. Those parts with which we are here con-

cerned were not in existence, either at the time the testator made his will or when he died, nor did they constitute a restatement of previously expressed principles or rules. The testator could not, therefore, be deemed to have adopted and embodied them in his will, so that a change in such rules would defeat the disposition of his property which he intended to make by his will.

It would seem that some rules of administrative procedure may become so certain and definite and be accepted for such a length of time, that a testator or settlor may be deemed to have acted in reliance thereon in drawing his will or trust instrument and be said inferentially to have embodied them in his will or trust instrument, *American Security & Trust Co. v. Frost*, 117 Fed. (2d) 283, 285 (1940).

The *Chapal-Otis* rules had none of these characteristics.

At the time the testator executed his will, and at the time of his death, these *Chapal-Otis* rules had not even been enunciated. The only rules bearing upon this subject which had acquired any degree of certainty were (a) that expenses of foreclosure should be charged to capital, and (b) that, if real property so acquired was unproductive of income while held by a trustee, the proceeds of sale should be apportioned between principal and income; but the basis for that apportionment enunciated in the *Chapal-Otis* rules had not been established. In fact, the basis there stated was different from that which had been stated previously by the lower courts. *Roosevelt v. Roosevelt*, *supra*, and *Matter of Marshall*, *supra*. With respect to the rents from such a property, there was no suggestion that they should be treated differently than the rents from any other property. In the only case where such rents were considered, it had been recognized that they had been properly treated as income. *Van Vleck v. Lounsbery*, *supra*.

That these *Chapal-Otis* rules were mere rules of administration and that the Court of Appeals understood them to be such, is shown, not only by the statement of the court in *Matter of Otis* (p. 115), but also in the court's refusal to follow established equitable doctrine in their formu-

lation. Apparently, it believed that the application of accepted equitable principles would prove impractical to deal with the countless properties which had been acquired by trustees on the foreclosure of mortgages, and therefore, promulgated rules "shaped by considerations of business policy" "in the endeavor to express fair, convenient, practical guides that [would] be largely automatic in their application," and expressly declared that they should not be regarded as "final for all cases" (276 N. Y. 115).

When a trustee buys in the underlying property on foreclosing a mortgage, he holds the land upon a trust "implied" or "created by law" to sell the property and reconvert it into personalty. *Lockman v. Reilly*, 95 N. Y. 64.

There were, therefore, available to the court in the solution of the various questions arising in connection with such foreclosed property, all the equitable principles theretofore established with respect to the express trusts to sell real property, invest the proceeds and distribute the income and principal. The rules which had been evolved in connection with these trusts were well defined. Expenses in excess of rents were payable from capital. *Furniss v. Cruikshank*, 230 N. Y. 495, 510 (1921). If the rents collected did not represent an adequate income, then the proceeds of sale, plus any rents received, were distributable between income and principal. In the determination of the proportionate share of income, interest was to be computed at the equitable rates, i. e., that prevailing for trustee's investments during the period that property was held after the duty to sell arose. *Laurence v. Littlefield*, 215 N. Y. 561, 583 (1915). *Furniss v. Cruikshank*, *supra*, 509; *Restatement of the Law of Trusts*, Sec. 241.

Any rents distributed as income would of course be deductible from income's share. *Restatement of the Law of Trusts*, Sec. 241, Comment d.

Principal's share was that amount which with interest at such rate would equal the net proceeds of sale. *Laurence v. Littlefield*, *supra*, *Furniss v. Cruikshank*, *supra*, *Matter of Jackson*, 258 N. Y. 281 (1932).

The lower courts of New York had applied these principals to foreclosed properties, *Roosevelt v. Roosevelt*, 5 Redf. 264 (N. Y. Co. Surr. Ct., 1881), and *Matter of Marshall*, 43 Misc. 238 (Kings Co. Surr. Ct., 1904).

The courts of other jurisdictions also applied these same principles. *Nirdlinger's Estate* (No. 2), 327 Pa. 171, 193 Atl. 30 (1937); *Springfield Safe Deposit & Trust Co. v. Wade*, 305 Mass. 36, 24 N. E. (2d) 764 (1940); *Quinn v. First National Bank*, 168 Tenn. 30, 73 S. W. (2d) 692 (1934); *Restatement of the Law of Trusts*, Sec. 241. In *Nirdlinger's Estate* (No. 2), *supra*, the Supreme Court of Pennsylvania also held that, if payments had been made from capital in connection with such a property, interest at the equitable rate should be computed not only on the principal amount of the mortgage, but also on all advances from capital. This was the rule enunciated by the surrogate in *Matter of Marshall*, *supra*.

It appears that the court rejected these familiar principles because it thought they would lead to complexity and uncertainty, and that a more practical guide should be involved, which would permit a trustee to deal with such problems without the aid of judicial instructions. In rejecting the calculation of interest at the equitable rate, and disallowing interest in all capital advances, it said, *Matter of Otis*, 276 N. Y. 101, 113, "Interest on each item would have to be computed at the currently prevailing rate for legal investments [those in which trustees are authorized to invest]—a fluctuating factor not readily ascertainable. The parties can hardly be thought to have contemplated such actuarial calculations."

In case of express trusts for the sale of property, it seems always to have been assumed that any net rents collected would be payable to the life beneficiary, and, therefore, there is little discussion of this subject either in the authorities or in the "Restatement of the Law of Trusts". Section 241 (d) of the latter gives implicit recognition that net rents should be paid to the life beneficiary, for it states that any interim payments to the life tenant shall be deducted from his share in the final apportionment.

The reason for this lack of discussion in the case of express trusts is not difficult to find. In New York, accumulations of income are not permitted except for a minor. No ingenious device to effect an accumulation indirectly, as by paying capital charges out of income, are permitted. *Hascall v. King*, 162 N. Y. 134. Therefore, a testator or settlor could not validly direct that until his real property be sold, all net rents therefrom should be accumulated to await distribution at that time. Under these circumstances, and in the absence of an express direction, it would be unreasonable to construe a trust instrument as impliedly directing that, if real property were bought in upon the foreclosure of a mortgage, any rents therefrom should be so accumulated. In fact, it would seem that an express direction to this effect would be held invalid for there is no reasonable distinction between an express and implied trust for the sale of real property.

It seems obvious that the *Chapal-Otis* rules were not intended to be and should not be accorded the dignity of rules of property. They were "practical guides" shaped by "considerations of business policy", and not based on accepted equitable principles, and they were enumerated by the court as tentative rules, with the express statement that they were not to be considered "final for all cases". As was well said in *United States v. Standard Oil Company of California*, 20 F. Supp. 427, 458, aff'd 107 F. (2d) 402, cert. denied 309 U. S. 673:

"However, before setting up a judicial declaration as a rule of property, we should require, at least, that it be fixed, long-continued, and relied upon by persons acquiring property, so that its repudiation would amount to a denial of due process."

Certainly, rules not formulated until 1936 and 1937 cannot be considered rules of property affecting a will drawn in 1928 by a testator who died in 1934.

The argument that the statute is unconstitutional rests on the proposition that it transfers the property of the remaindermen to the life beneficiary. To determine the rights of the life beneficiary and remaindermen, we turn to



the will, the source of their title. Here we find merely a bequest of the net income of the trust to one and of principal to others.

Even if we assume *arguendo*, that under the *Chapal-Otis* rules, no part of the rents would have been payable to the widow until all capital advances had been repaid, we must remember that these rules were not in existence when the will took effect. Since the will indicates that the testator's widow was the primary object of his bounty, we may appropriately conclude that, if the application of the *Chapal-Otis* rules would have the effect of depriving her of the income from a large part of the principal of the trust for an extended period, and that the statute changed these rules so as to restore to the widow some of that income, the statute tends to give effect to the testator's intent rather than to defeat it. It follows, therefore, that any argument that the statute transferred to the widow property given by the testator to the remaindermen is wholly fictitious.

(d)

The beneficiaries of a trust have no vested right in the maintenance of any rules of administrative procedure with respect thereto.

None has a vested right in the maintenance of any rules of procedure. There is no constitutional limitation against a change of such rules even if such change is applicable to existing contracts or property. The mere fact that a change in such rules may result in decreasing the amount one would otherwise receive, or in increasing the amount one would otherwise be required to pay, is no impediment to such change being effected by legislation. *Preston Co. v. Funkhouser*, 261 N. Y. 140, affirmed 290 U. S. 163 (1933); *People ex rel. Eitel v. Lindheimer*, 371 Ill. 367, 21 N. E. (2) 318, 308 U. S. 505 (1939); *Carpenter v. Wabash Ry. Co.*, 309 U. S. 23 (1940).

As we shall show hereafter, rules with respect to the administration of trusts are regarded as rules of administrative procedure possessing the same characteristics as



other rules of procedure, in that they are subject to legislative change.

(e)

The statute did not reduce the amount which might have been paid either to the remaindermen or life beneficiaries of trusts under the *Chapal-Otis* rules.

The argument of unconstitutionality proceeds on the assumption that, under the statute, the remaindermen will or may receive less than they would be entitled to under the *Chapal-Otis* rules. It is based upon the appellant's contention concerning the proper interpretation of those rules. Such argument was doubtless one which was appropriately addressed to the court below, but hardly here, for we assume that this court will accept the Court of Appeals' interpretation of the meaning and effect of the rules which that court promulgated.

It was urged in the Court of Appeals, as it is argued here, that under a proper interpretation of the *Chapal-Otis* rules, no surplus rents could be paid to a life beneficiary until all capital advances had been repaid, and that if enough were not realized upon the sale of the property to repay such capital advances, all surplus rents as might be necessary must be used for such purpose.

However, the majority of the court held that, under the *Chapal-Otis* rules, a trustee had discretion to distribute surplus rents, and that if in exercise thereof he paid such rents to a life beneficiary, he would not have been liable to surcharge therefor. The court said, referring to its opinion in the *Otis* case (R. 120):

"It was also carefully pointed out that no hard and fast rule was laid down to guide the trustee in the disposition of net income earned during the salvage operation, but the disbursement of net income to the life beneficiary was left to the discretion of the trustee."

It also said (R. 121):

"In thus formulating a rule that is final against recoupment for distribution of income received in excess of carrying charges, it does not appear that the Legislature has done more than direct a trustee to do what under the decisions of this court he has discretionary power to do. (*Matter of Otis, supra.*) Before the enactment of this statute, the life tenant could not have demanded as of right the payment to him during liquidation of more of the surplus income than he will receive under the statute. Neither does it appear that the remaindermen could properly have insisted that the trustee should be surcharged if in the exercise of his discretion he had paid to the life tenant the amount which the statute now directs. A statutory rule of administration which requires the trustee to apportion income in accordance with a fixed standard which in the exercise of administrative discretion the trustee would even without the statute have power to adopt does not, in our opinion, constitute a taking of property."

## II

**The New York State Legislature had power to enact the remedial statute in question. It is in all respects reasonable and does not violate the Fourteenth Amendment to the Constitution.**

### (a)

Under the law of New York, the legislature may make and modify rules of administrative procedure affecting trusts.

In New York, both the courts and the legislature have taken part in the formulation of rules for the administration of trust estates. They are not rules of law resting upon matters of public policy. They are merely rules for the guidance of trustees with respect to matters upon which

the testator or settlor has given no express direction. A testator or settlor may, therefore, direct, that a different rule than that which has been formulated by the courts or the legislature shall be followed by his trustee (*Crabb v. Young*, 92 N. Y. 56, 65; *Matter of Reid*, 170 App. Div. 631, 634, aff'd. 218 N. Y. 640).

Courts of equity established rules with respect to the investments which might properly be made by a trustee (*King v. Talbot*, 40 N. Y. 76, 83 (1869)). These rules have been repeatedly modified by statute, and these modifications have been held to apply to existing trusts (*City Bank Farmers Trust Company v. Evans*, 255 App. Div. 135, 1938; *Matter of Hammersley*, 152 Misc. 903, 1934). Obviously the character of the investments will, to a large extent, determine the amount of income of the life beneficiary and the amount of principal which may remain for distribution upon the termination of the trust.

Under the former chancery rules prevailing in New York, neither executors nor trustees were entitled to any compensation for their services, but when an act was passed in 1817 authorizing the courts to make an allowance to executors, administrators, and guardians, upon the settlement of their accounts, for services in the discharge of their trusts, it was held that the statute was retrospective in its operation and was intended to embrace cases where the services had been performed before the passage of the statute, if the settlement of the account took place afterwards (*Dakin v. Demming*, 6 Paige Ch. 95, 1836).

It has since been definitely established by the New York courts that the legislature may modify the rules with respect to the allowance of commissions to trustees with respect to trusts theretofore established (*Matter of Barker*, 230 N. Y. 364, 1921; *Robertson v. DeBrulatour*, 188 N. Y. 301, 316, 317, 1907). Although commissions of trustees were substantially doubled by a statute enacted in 1916, it was held in *Matter of Barker, supra*, that the new rates of commissions were applicable to existing trusts.

In 1914, what is now Section 225 of the Surrogate's Court Act was enacted, providing, "Where power to mort-

gage, lease or sell real estate is given by a will to an executor or trustee, an administrator with the will annexed or a successor trustee may execute such power in any case where the original executor or trustee could execute the same, unless contrary to the express provisions of the will."

In *Hollenbach v. Born*, 238 N. Y. 34, 1924, the application of this section to an administrator with the will annexed, who was appointed after that section took effect, under a will which had been probated long prior thereto, was challenged. Although recognizing that before the passage of this act an administrator with the will annexed could not have exercised a discretionary power of sale, the court upheld the application of the statute on the ground that the statute did not change "existing substantive rights".

Similarly, Sections 67-71 and Sections 105-107 of the New York Real Property Law, authorizing the Supreme Court to direct a sale or to empower a trustee to mortgage or sell real property, have been held to apply to existing estates (*Matter of Mersereau*, 233 N. Y. 540, 1922), and this notwithstanding a testamentary direction that the real property should not be sold (*Matter of O'Donnell*, 221 N. Y. 497, 1917).

The legislature has on many other occasions enacted statutes modifying other rules of administration which have been established by the courts, but we omit reference thereto as the validity of these statutes seems to have been recognized without litigation.

Thus it appears to be the established law of New York that if substantive rights are not disturbed, the legislature is free to change the rules of administration with respect to trusts; further that in some respects the powers of the legislature with respect to trusts are more extensive than are those of the courts.

In *Clarke vs. Van Surlay*, 15 Wend. 436, aff'd 20 Wend. 365 (1836), the court upheld a private statute appointing a new trustee and authorizing the trustee so appointed to sell the real property constituting the trust. The court, referring to Blackstone's Commentaries, held that such power

had existed in Parliament and that it existed in the legislature of the state of New York. With respect to the appointment of a trustee, the court said (p. 442):

"There can be little doubt that the court of chancery, without an act of the legislature, could have discharged the trustees selected by the testatrix, and appointed others in their place; and although the expediency of changing the trustees by law, instead of leaving it to the chancellor, may be questioned, it was not an act beyond the power of the legislature. The mere substitution of a new trustee could neither defeat the trust nor divest the rights of those beneficially interested in the property."

As above stated, in New York these rules affecting the administration of trusts have been treated as rules of procedure. In *Matter of Barker*, *supra*, 230 N. Y. 364, where the court held that a statute increasing the compensation of trustees was applicable to an existing trust and to the allowance of commissions for services theretofore rendered, the court said (p. 372):

"The general rule is that the fees of an executor are to be fixed by the rules and law which prevail at the time when they are settled. (*Robertson v. de Brulattour*, 188 N. Y. 301, 316, 317; *Whitehead v. Draper*, 132 App. Div. 799.) In the last case this principle was applied in the opinion written by Justice McLAUGHLIN in a case where the statute invoked in aid of an executor's commissions was not passed until after his death. This is quite akin to the rule that remedies will be applied in accordance with the law which prevails at the time when relief is sought rather than at the time when the injury arose."

In *Matter of Potter*, 106 Misc. 113 (1919), where the same statute was considered, the court said:

"Acts relating to procedure are therefore not retroactive in the sense that they relate back to and modify a pre-existing state of right. Rather are they prospective since they apply only to a ruling to be made in the future, albeit with respect to transactions in the past which come up for adjudication in the future."

Doubtless this treatment of rules of administration arises from the fact that the administration of trusts is always subject to the supervision of the chancellor or the courts which have been authorized to exercise the chancellor's powers, and all questions, as to whether a trustee has followed the correct rules of administration, are tested in an action or proceeding where these rules are applied. Those cases dealing with the award of compensation involve this principle. Commissions are awarded in a proceeding for the settlement of the trustee's accounts.

(b)

This court will not disturb the determination of the New York Court of Appeals concerning the power of the State legislature to enact the statute in question. It will confine its inquiry to the question whether, in exercising that power, the legislature violated any provision of the Federal Constitution.

The question discussed by LEWIS, J. (R. 126-7), in his dissenting opinion in the Court of Appeals, concerning the power of the legislature to modify rules of administration with respect to existing trusts, was doubtless a proper subject for consideration by the State courts. So also was the question as to whether the statute violated the State Constitution, it having been contended by the appellants that the statute violated the provisions of both the Federal and State Constitutions (R. 79). This court, however, will not disturb the determination of the court below that, under the state law, the legislature had power to enact the statute, and that it did not violate the State Constitution (*Terrace vs. Thompson*, 263 U. S. 197, 224; *Giozza vs. Tiernan*, 148 U. S. 657, 661).

(c)

Because of the uncertainty in the correct rules of administrative procedure and the consequent hardship on income beneficiaries, it was most appropriate for the legislature to enact the statute in question.



The object of the statute was to provide a definite rule under which trustees might distribute to life beneficiaries rents collected upon properties which had been acquired upon foreclosure. Before the enactment of the statute such rules as had been established were so indefinite and uncertain that life tenants were deprived of any income during indefinitely extended mortgage salvage operations.

The state of the New York law before the *Chapal* and *Otis* decisions in the Court of Appeals is graphically stated by the Surrogate in *Matter of Pelecyger*, 157 Misc. 913, 915 (1936), as follows:

"Unfortunately, as will hereinafter appear, the rules of conduct in such situations, heretofore formulated by the courts, are in somewhat serious conflict, with the result that the legion of affected interests has been compelled to flounder in semi-darkness with no adequate judicial guidance to illuminate the path which they should pursue."

In *Matter of Chapal* the court left undetermined various questions including the question as to the distribution of income. In *Matter of Otis* it was stated that a trustee had some undefined discretion to distribute income received during the salvage. As the Executive Committee of the Surrogates' Association informed the legislature: "Trustees have hesitated to pay such net income because in the case of overpayment to the life tenant, the trustee might be surcharged with that amount."

It was to overcome this uncertainty in the law that the legislature acted. It sought to simplify "the rules of procedure in mortgage salvage operations and the elimination of present complications which work to the disadvantage of the life tenant \* \* \*." (Sub-paragraph (d) of subdivision 2 of the statute.)

There can be no doubt but that the uncertain and unsatisfactory state of the law presented an appropriate subject for legislative action. This is well illustrated by *Funkhouser v. Preston Co.*, 290 U. S. 164. There considered was the New York statute providing for the recovery of interest upon principal sums awarded in actions for breach of con-

tract without regard to whether the principal sum was liquidated or unliquidated. The constitutionality of the application of the statute to a pre-existing obligation was questioned. Because the New York law before the enactment of the statute was "not clear and certain" (290 U. S. at 166), this Court said that—

"Without attempting to review the numerous, and not harmonious, decisions upon the allowance of interest in the case of unliquidated claims, it is sufficient to say that the subject is an appropriate one for legislative action in order to provide a definite rule." (168)

*Kuehner v. Irving Trust Company*, 299 U. S. 445, involved the constitutionality under the Fifth Amendment of Subdivision (b) (10) of Section 77B of the Bankruptcy Act limiting landlords' claims in proceedings under that section to an amount not to exceed three years' rent. This Court in upholding the statute said (p. 453);

"It gave a new and more certain remedy for a limited amount, in lieu of an old remedy inefficient and uncertain in its result."

Clearly the New York Legislature in enacting Subdivision 2 of Section 17-c was acting within the scope of its legislative authority. As heretofore set forth, the statute took away no vested right and deprived none of any property. In the enactment of the statute the legislature merely performed its proper function to remedy a defect in the common law (*Munn v. Illinois*, 94 U. S. 113, 134) and to supply a definite rule for one that was indefinite and uncertain (*Funkhouser v. Preston Co.*, *supra*). Since the statute has "a reasonable relation to a proper legislative purpose", it is not to be condemned, unless it is arbitrary or discriminatory (*Nebbia v. N. Y.*, 291 U. S. 502, 537; *Kuehner v. Irving Trust Co.*, *supra*, 455).

(d)

The statute is not arbitrary or capricious, but on the contrary is fair and reasonable and was designed to protect

both the interests of the life beneficiaries and remaindermen. Its validity should, therefore, be sustained.

The statute expressly preserves the rule of apportionment previously established by the courts. No effort was made to change the amount that ultimately would be paid either to the life beneficiary or remainderman. It merely provides for a regular and orderly distribution of part of the income from a foreclosed property pending a resale by the trustee. It displaces uncertainty with certainty. Instead of requiring the trustee to exercise discretion, without any guiding chart, as to whether he should or should not distribute income to a life beneficiary, it supplies a definite rule. True, it does not require that all the net income first received shall be used to repay capital charges, but it protects those interested in the capital of the trust by specifically providing that any capital charges not repaid out of the income "shall be a primary lien upon the proceeds of sale and shall be paid first out of any cash so derived. If insufficient the balance shall be a primary lien upon any purchase money mortgage received upon the sale." [Sub-paragraph (c).]

The statute shows meticulous care to preserve a nice balance in establishing a rule which would be fair not only to the life beneficiary but to remaindermen. Under the statute, a life beneficiary can receive nothing pending a resale of the property unless it produces net income. If it does produce net income in any year, the trustee is not permitted to pay all of that to the life beneficiary, but only three per cent of the principal of the mortgage. All surplus income above such three per cent must be impounded to await a resale of the property.

In determining the reasonableness of the statute, the court may appropriately take cognizance of the fact that the rules established with respect to such salvage operations in other states, without the aid of any statute, are doubtless more favorable to life beneficiaries than are rules established by the statute here in question. We have already alluded to the authorities of other states (*supra*, page 17). In addition to what is there stated, it may also be noted that

the Supreme Court of Pennsylvania determined that if the proceeds of sale consist in part of a purchase money mortgage, any cash received on the sale must be used to pay the deferred income to which the life beneficiary is entitled (*Re Nirdlinger's Estate*, 327 Pa. 171, 193 Atl. 30, 35).

The appellant refers to the statement found in subdivision (d) of the statute, that the life tenant "is usually the principal object of the testator's or settlor's bounty", and asserts that the legislature has interpreted the intent of each and every testator who died prior to the enactment of the statute, and whose estate contained a salvage operation. Obviously, the legislature did not find that the life beneficiary is always the chief object of the testator's bounty, but merely that this is usually so. That was the opinion of the Executive Committee of the Surrogate's Association as expressed in its report to the legislature, and surely there is none better able to form an opinion upon that subject than the surrogates. As we have seen, it was true in the instant case. At least, it is clear that the Legislature was not unreasonable in determining that creators of trusts, having directed the payment of income to life beneficiaries, meant that their direction to pay income should be followed.

In establishing a general rule, the legislature was required to consider the usual, and not the exception. As stated by the court in *Home Bldg. & L. Association v. Blaisdell*, 290 U. S. 398, 446, "It does not matter that there are, or may be, individual cases of another aspect. The legislature was entitled to deal with the general or typical situation."

The appellant particularly stresses the provisions of the statute to the effect that if, upon the final liquidation, it appears that the amount of surplus rent paid to the life beneficiary is in excess of the life beneficiary's share of the total amount realized in the salvage operation, i. e. the surplus rents plus the proceeds of sale, there is to be no recoupment from the life tenant.

This is in no way improper or unusual. The legislature might have gone further than to provide merely that the surplus rents in any year up to three per cent of the prin-

cipal of the mortgage should be deemed income. It might have provided that all surplus rents should be deemed income and be distributed as such. Traditionally, rent has always been regarded as income, and traditionally, income cannot be recaptured merely because the principal investment may be lost due to depreciation in value.

In *Dgett vs. Title Guarantee & Trust Company*, now pending before this court (No. 227, October term, 1943), it is asserted that if the provisions of Section 17-e are applied, the final liquidation will not produce a sum sufficient to pay all capital advances. That result is not to be attributed to the fact that rent was received and paid to the life beneficiary, but rather to the depreciation in the value of the property after the inception of the salvage operation, or to improvidence on the part of the trustee in attempting to salvage an investment when there was no equity to salvage.

As heretofore indicated, the statute may not be condemned, because in some instances a slightly different result may occur from its application than that which would have occurred had the statute not been enacted.

### Conclusion

The validity of the statute should be sustained. It was within the power of the legislature of New York to enact it. The statute is in all respects reasonable and appropriate to accomplish its purpose to remedy the defects in the rules of administration which had been tentatively promulgated by the courts. It deprives none of any property without due process of law.

Respectfully submitted,

C. ALEXANDER CAPRON,

*Counsel for Respondent Trustee.*

J. KARR TAYLOR,

J. DINSMORE ADAMS,

*Of Counsel.*

# SUPREME COURT OF THE UNITED STATES.

Nos. 52 and 227.—OCTOBER TERM, 1943.

William J. Demorest, Jr., Ann Demorest  
and Carolyn Demorest by Francis J.  
Mahoney, their Special Guardian, Ap-  
pellants,

52

vs

City Bank Farmers Trust Company, as  
Trustee under the Will of Henry C.  
West, Deceased, et al.

On Appeals from the  
Surrogate's Court of  
New York County,  
State of New York.

Thomas B. Dyett, Special Guardian for  
Joachim Heinrich Schmidt, Appellant,

227

vs.

Title Guarantee and Trust Company,  
et al.

[January 17, 1944.]

Mr. Justice JACKSON delivered the opinion of the Court.

Appellants in these two cases challenge the constitutionality of Subdivision 2 of § 17-c of the Personal Property Law of the State of New York; approved April 13, 1940.<sup>1</sup> Because of retroactivity it is said to offend the Due Process Clause of the Fourteenth Amendment to the Federal Constitution by taking for benefit of income beneficiaries property to which the appellants as bene-

<sup>1</sup> N. Y. Laws 1940, c. 452, p. 1182. The subsection provides:

"2. The existing rules of procedure applying to salvage operations respecting existing mortgage investments are continued except as modified by the subparagraphs hereinafter set forth. The terms and rules of procedure of this subdivision shall apply specifically (a) to the estates of persons dying before its enactment and (b) to mortgages on real property held by a trustee under a deed of trust or other instrument executed before the date of its enactment and (c) to real property acquired by foreclosure of mortgage or real property acquired in lieu of foreclosure before or after the date of its enactment in trusts created or mortgage investments made prior thereto, and (d) to any pending proceeding or action for an accounting of the transactions of an executor or trustee.

"(a) Net income during the salvage operation up to three per centum per annum upon the principal amount of the mortgage shall be paid to the life tenant, regardless of principal advances for the expenses of foreclosure or of



ficiaries of principal claim vested rights. It is asserted, also, to deny equal protection of the laws.

The facts in No. 52 are these: Henry West died in 1934. His will, so far as concerns us, left a residuary estate in trust. Net income less certain payments to a brother was given to his wife during her life or widowhood. Thereafter, subject to certain further trusts, the residue was to go to contingent remaindermen, among whom are the appellants.

At death West owned a number of mortgages. Owing to defaults, titles to nine of the underlying properties were acquired either by foreclosure sale or by deed in lieu thereof, and held in separate accounts as assets of the trust. The trustee's accounting disclosed that two such salvage operations were completed by sale of the properties prior to the enactment of § 17-c of the Personal Property Law. No distribution had been made of the proceeds. Objections on behalf of remaindermen questioned the validity of the statute as applied to apportioning such proceeds between income and principal. Surrogate Foley, however, upheld the

conveyance in lieu of foreclosure and arrears of taxes and other liens which occurred prior to such foreclosure or conveyance and the cost of all capital improvements. Any payment of net income heretofore or hereafter made to the life tenant up to such three per centum per annum shall be final and shall be not subject to recoupment from the life tenant or as a surcharge against the trustee or executor. The amount of all such payments shall be taken into account, however, in the apportionment of the proceeds of sale and shall be charged against the share of the life tenant.

"(b) The foregoing principal advances shall be repaid out of excess net income above such three per centum per annum. When principal advances have been satisfied, any excess income shall be impounded (subject to reinvestment under the terms of the will or deed) to await sale and apportionment.

"(c) The unpaid principal advances shall be a primary lien upon the proceeds of sale and shall be paid first out of any cash so derived. If insufficient the balance shall be a primary lien upon any purchase money mortgage received upon the sale.

"(d) The purpose of the enactment of this subdivision is declared to be the simplification of the rules of procedure in mortgage salvage operations and the elimination of present complications which work to the disadvantage of the life tenant, who is usually the principal object of the testator's or settlor's bounty, by depriving him of a fixed right to the actual payment of any net income earned by the property. Such fixed right is granted in lieu of the discretion now given to the trustee to pay net income or any part thereof to the life tenant. The general rules of the apportionment of the proceeds of sale between life tenant and remainderman are retained subject to the express modifications made herein. Only equitable adjustments and balances as between the parties are intended to be effectuated by the provisions of this subdivision. If any provision of this subdivision or the application thereof to any mortgage or acquired property by foreclosure or conveyance, or to any trust is held invalid, the remainder of the subdivision and the application of such provision to any other mortgage or property acquired by foreclosure or conveyance or other trust shall not be affected thereby.

statute and resolved the apportionment under its terms. His decree was unanimously affirmed by the Appellate Division of the Supreme Court for the First Judicial Department and thereafter was affirmed by the Court of Appeals, two judges dissenting. *Matter of West*, 289 N. Y. 423. The case is brought here by appeal.

In No. 227, Auguste Schnitzler died in 1930, leaving a will which put her residuary estate in trust with the income payable to a sister for life. The income beneficiary died in 1939. Salvage operations had begun in the lifetime of the beneficiary and were completed after her death. Surrogate Delehanty found that operation of the statute "resulted over the whole salvage period in taking for income account more than the whole of what the property earned in that period. The deficit in so-called 'income' was made up by taking principal, of course." He considered the result "startling" but settled the accounts under the statute, leaving its validity to be determined by appellate courts. The Court of Appeals affirmed without opinion on the authority of *Matter of West* and the case comes here by appeal.

The grievance of remaindermen in these cases is not that they have suffered loss or deprivation of any specific property to which they had legal title. Under the law of New York the whole legal estate vests in the trustee for purposes of the trust,<sup>2</sup> including title to mortgages and to real estate acquired upon or in lieu of their foreclosure, which becomes personalty for the purposes of the trust.<sup>3</sup> Where the instrument creating the trust directs payment of income to one set of beneficiaries and corpus to another, allocation of receipts and disbursements as between capital and income is sometimes attended with difficulty. Mortgage investments may be imperiled by default in interest only, or payments of principal alone, or of both, but in either event both income and capital interests require protection. Advancements often must be made to remove tax liens or other prior charges, pay costs of foreclosure, make property tenantable, or take care of operating losses, watchmen, or insurance. On final sale the price, together with rentals, may leave either a loss or a profit, and to forego income for a period may result in a better sale of the capital asset. The variety of circumstances under which trustees are called upon

<sup>2</sup> *Knox v. Jones*, 47 N. Y. 389; *Bennett v. Garlock*, 79 N. Y. 302. Cf. 1 Scott on Trusts, p. 3.

<sup>3</sup> *Lockman v. Reilly*, 95 N. Y. 64.

to allocate items between capital and income are innumerable in salvage operations, the will rarely provides guidance, and the wisest and most faithful trustee is unable to draw the line with any great assurance. Either the income beneficiary or the remaindermen may challenge his accounts, for they have equitable interests which chancery will enforce that the trust be administered diligently and faithfully according to the will and the law. The flood of issues as to allotment of receipts and disbursements to capital or income account, following the depression, led the Court of Appeals to attempt to clarify the chancery rules on the subject for better guidance of trustees and the courts that supervise them.<sup>4</sup> When this was only partially successful, the problem of clarification was carried further by legislation. The remaindermen claim an unconstitutional taking of their property results from this legislative enactment of rules for distribution as between income and capital beneficiaries of trust property involved in salvage operations, because they are less favorable to the remainder interests in these cases than the rules they claim otherwise would have applied.

Appellants' contention is that the New York Court of Appeals established a rule of apportionment of proceeds of salvage operations of mortgaged property as between income and principal which became a settled rule of property under which property rights vested in them prior to accounting by the trustees. This, they say, was accomplished by the decisions in *Matter of Chapel*, 269 N. Y. 464 (1936), and *Matter of Otis*, 276 N. Y. 101 (1937). The Court of Appeals, however, in one of the present cases holds to the contrary, saying that these opinions represent tentative judicial efforts to guide the discretion of trustees; that they did not establish rules of property; and that the legislature appears to have done no more than to direct trustees to do what they already had discretion to do, in which case remaindermen could not have insisted upon their being surcharged under the law before the enactment.

In thus rejecting appellants' version of its previous decisions the Court of Appeals disposed of their cases on the ground that appellants have never possessed under New York law such a prop-

<sup>4</sup> In New York, power to "direct and control the conduct, and settle the accounts" of trustees is allotted to the Surrogate's Court. Surrogate's Court Act § 40(3).

erty right as they claim has been taken from them. If this is the case, appellants have no question for us under the Due Process Clause. Decisions of this Court as to its province in such circumstances were summarized in *Broad River Power Co. v. South Carolina*, 281 U. S. 537, 540, as follows: "Whether the state court has denied to rights asserted under local law the protection which the Constitution guarantees is a question upon which the petitioners are entitled to invoke the judgment of this Court. Even though the constitutional protection invoked be denied on non-federal grounds, it is the province of this Court to inquire whether the decision of the state court rests upon a fair or substantial basis. If unsubstantial, constitutional obligations may not be thus evaded. But if there is no evasion of the constitutional issue, and the non-federal ground of decision has fair support, this Court will not inquire whether the rule applied by the state court is right or wrong, or substitute its own view of what should be deemed the better rule, for that of the state court."<sup>5</sup>

Despite difference of opinion within the Court of Appeals as to the effect of its earlier cases, we think that the decision of the majority that they did not amount to a rule of property does rest on a fair and substantial basis. The opinion in the *Otis* case had indicated a tentative quality in its pronouncements, saying: "Perhaps it should be added that a general rule for such situations cannot be attained at a bound, that no rule can be final for all cases and that any rule must in the end be shaped by considerations of business policy. Accordingly, we have here put aside inadequate legal analogies in the endeavor to express fair, convenient, practical guides that will be largely automatic in their application. Only the sure result of time will tell how far we have succeeded." And the opinion had pointed out that the disbursement of net income during salvage operations was left to the discretion of the trustee with the admonition that the discretion "should be exercised with appropriate regard for the fact that unless a life tenant gets cash he does not get anything in the here and now." 276 N. Y. 101-115.

<sup>5</sup> See same case on rehearing, 282 U. S. 187, and *Sater v. New York*, 206 U. S. 536, 540; *Leathe v. Thomas*, 297 U. S. 93; *Vandalia Railroad Co. v. Indiana*, 207 U. S. 359, 367; *Enterprise Irrigation Dist. v. Farmers Mutual Canal Co.*, 243 U. S. 157, 164; *Ward v. Love County*, 253 U. S. 17, 22; *Fox River Paper Co. v. Railroad Commission*, 274 U. S. 651, 655. Compare *United Fuel Gas Co. v. Railroad Commission*, 278 U. S. 300, 307; *Risty v. Chicago, Rock Island & Pacific Ry. Co.*, 270 U. S. 378, 387.

The executive committee of the Surrogates' Association of the State of New York, composed of the judicial officers immediately charged with application of these decisions to the instruction of and accountings by trustees held a similar view of the discretion left to trustees. The legislature appears to have been of the same mind in adopting the new legislation.<sup>6</sup> The judicial effort was to formulate general rules to guide fiduciary discretion. The *Chapal* decision was rendered in response to a trustee's petition for instructions. But while such decisions were useful as precedents

<sup>6</sup> When it was introduced into the legislature, the bill proposing § 17-c carried the following explanatory note by the Surrogates' Association:

"This amendment is proposed by the executive committee of the Surrogates' Association of the state of New York. Its general purposes are:

"(1) To simplify the complicated rules restated in *Matter of Chapal* (269 N. Y. 464) and in *Matter of Otis* (276 N. Y. 101) relating to mortgage salvage operations (a) in existing trusts as to mortgages hereafter acquired as a trust investment and (b) in testamentary trusts created by the will of decedent dying after its enactment and (c) in *inter vivos* trusts created by an instrument executed after its enactment. Such simplification is provided in the first subdivision of the new section.

"In recent years section 17-a of the Personal Property law was enacted to avoid the difficult problems of the allocation of stock dividends received during the period of a trust. Under that section they are now allocated wholly to capital. Section 17-b of the Personal Property law was enacted to abolish the intricate rule in *Matter of Benson* (96 N. Y. 499) under which it was necessary to capitalize the income on monies held within the estate for the payment of administration expenses, debts, taxes and pecuniary legacies. In line with this policy the proposed legislation contained in the first subdivision abolishes in the instances stated above, the *Chapal-Otis* rules, and will substitute a simple form of the treatment of the foreclosed real property as a principal asset of the trust. It is to be treated just as a railroad bond upon which default in interest before sale has occurred.

"(2) Further modifications are proposed by the second subdivision of the section as to mortgage investments already made in existing trusts. The present rules for apportionment between life tenant and remainderman under the *Chapal-Otis* cases are continued as to existing trusts where the investment in a mortgage has been made, with modification thereof in two specific instances.

"(a) The *Chapal-Otis* rule authorizes the trustee to pay surplus net income in his discretion. Trustees have hesitated to pay such net income because in the case of overpayment to the life tenant, the trustee might be surcharged with that amount. The life tenant of the trust must wait in the majority of cases for a long period of time before he becomes entitled to the payment of any income, because of the present requirement that advances from principal for the expenses of foreclosure and for arrears of taxes and other liens must first be paid from the net income of the property. The amendment provides for the immediate payment of income to the life tenant beginning with the date of the acquisition of the property by the trustee by foreclosure or conveyance in lieu of foreclosure. Under the new provisions net income up to three per centum of the face amount of the mortgage is so payable. Under the *Chapal-Otis* rules the life tenant is entitled in the final apportionment to the inclusion of interest at the mortgage rate during the period of the salvage operation. The rate of three per centum in the new section has been recom-



dents, they were felt not adequate to protect trustees against the hazards of litigation in particular cases, and the avowed effort of the court to adapt the law to the situation resulting from the depression failed in practice.<sup>7</sup> Hence the legislature intervened, adopted a rule which the trustee might have applied before, in its discretion, and prescribed it as a definite standard for setting apart income, protecting trustees against liability to remaindermen if they followed it. What appears really to have been taken from the remainderman is his right to question the equity of the rule in his individual circumstances, a right which he had while it was a rule of the court. In the case of the *Schnitzler* trusts where the rule results in invasion of the remainderman's principal to make good to the life beneficiary the statutory allowance of income, Surrogate Delehanty implied, and no one has de-

mended as a fair return to the life tenant and at the same time a protection to the remainderman in the event that the property is sold at less than the face amounts of the income and principal shares employed as the ratio of the apportionment. (b) Surplus net income above three per centum is to be applied to the payment of advances from principal until the amount of such advances are satisfied. When the property in the salvage operation is sold, the unpaid balance of principal advances must be satisfied first out of the cash received from the sale. If there be any unpaid balance due for principal advances, it is made a primary lien upon the purchase money mortgage. The amendment further directs that after principal advances have been paid, the surplus net income above three per centum, accruing during the salvage operation, shall be held by the trustee to await sale and apportionment under the *Chapal Otis* rules.<sup>8</sup> N. Y. Laws 1940, p. 1181.

<sup>7</sup> Surrogate Foley in the *Demorest* case states the effect of this Act as follows (*Matter of West*, 175 Misc. 1044, 1048):

"Two relatively simple modifications of the *Chapal Otis* rules were made in this subdivision. Under those rules and particularly under the language of the opinion of Judge Loughran in *Matter of Otis* (*supra*), a discretionary power was given to a trustee during a mortgage salvage operation to disburse income to the life tenant, after advances made from principal as an incident to the acquisition of the property had been repaid. It was found, however, that trustees hesitated to make any payment to the life tenant or to exercise the judicial discretion given to them by *Matter of Otis*, because of the fear of a possible surcharge in the event of an overpayment to the life tenant. The life tenant in almost every instance was the primary object of the testator's bounty. The beneficiary intended to be most favored was thus deprived by the trustee's inaction or hesitancy, of receiving income during the entire salvage period and large sums of money were accumulated and frozen. The injustice to the life tenant was aggravated by the fact that because of the lack of a ready market for the resale of the property, the salvage operation was unduly extended for a long period of years. This situation is emphasized by the facts revealed in the present proceeding. Of the seven mortgages now involved in the salvage operations in which no resale has taken place, the longest period of operation has been six years and two months. The shortest period has been four years and ten months. Thus the average period of operation of all seven mortgages has been approximately five years. In the two completed operations the periods of salvage were two years and six months and two years and eight months. This unhappy situation has been



nied, that the flexibility of the former rule would probably have resulted in a surcharge of the trustee's accounts, and hence that the remainderman has been deprived of the value which benefit of the *Chapal-Otis* rule would likely add to his remainder. Of course the very purpose of the statute, as Surrogate Foley points out, is to deprive him of that objection to the accounts, to protect the trustee against that hazard, and to give the remainderman other compensatory advantages. The legislature has furthered certainty at cost of flexibility.

Constitutional validity of this legislation if it had been made applicable to estates of decedents dying after its enactment is not questioned. It is objected only that application to an estate whose administration began before the Act so as to take away the remainderman's right to judicial examination of the trustee's computation of income makes it void for retroactivity.

It may be observed that insofar as appellants stand on the *Chapal-Otis* rule it can benefit them only if it may be retroactive. Both of these decedents died several years before either of those decisions. If a property right to some particular rule of income allotment in salvage proceeds vested at all, it would seem to have done so at death of the testator. If so, remaindermen would have to show that their property right was established by decisions then

corrected by the new legislation. Trustees are expressly authorized to pay promptly net income derived from the foreclosed or acquired property up to three per centum per annum upon the face amount of the mortgage. From the time of the passage of the new act, it has been the practical experience and observation of the surrogates that hundreds of thousands of dollars which had been theretofore accumulated, were paid out to life tenants upon the authority granted by the statute. Where the trustee had paid the yearly income up to the three per cent maximum to the life tenant, the statute made the payment final. It was specifically stated by the Legislature that such payment up to the maximum was 'not subject to recoupment from the life tenant or as a surcharge against the trustee or executor.' Moreover, under the new statutory rule, net income up to the maximum of three per cent became payable from the very beginning of the salvage operation, that is, from the date of acquisition by foreclosure or by deed in lieu of foreclosure.

"The other amendment to the *Chapal-Otis* rules made by the second subdivision of the new section in the balancing of the equities, furnished protection to the remaindermen interested in the principal of the trust. Excess net income earned in any one year during the salvage operation above the three per cent maximum payable to the life tenant, was directed to be applied to advancements from principal for arrears of taxes and other liens which accrued prior to the foreclosure or acquisition in lieu of foreclosure and to the cost of capital improvements. Where any balance of unpaid principal advances remained due at the close of the salvage operation, such balance was declared to be "a primary lien upon the proceeds of sale and shall be paid first out of any cash so derived. If insufficient the balance shall be a primary lien upon any purchase money mortgage received upon the sale."

in existence, or else that advantages derived from a later judicial decision may not be repealed. The case comes to this: Appellants took remainders at a time when the rules by which to sequester their interests in proceeds from complicated operations to salvage property were so indefinite that several years later the Court made an effort to devise more definitive rules for the purpose. They were but partly successful, and a few years later the legislature made further and perhaps more authoritative and final rules. Comparing the later with the earlier effort, the remainderman in these particular cases finds himself prejudiced. He says we must confirm him in the earlier by striking down the later of two retro-active rules of law.

This statute does not purport to open accountings already closed or to take away rights or remainders judicially settled under the old rule. The statute is applied only to judicial settlements pending at or instituted after its enactment. Rights to succession by will are created by the state, and may be limited, conditioned, or abolished by it. *Irving Trust Company v. Day*, 314 U. S. 556. The whole cluster of vexatious problems arising from uses and trusts, mortmain, the rule against perpetuities, and testamentary directions for accumulations or for suspensions of the power of alienation, is one whose history admonishes against unnecessary rigidity. The state may extend the testamentary privilege on terms which permit tying up of property in trust for possibly long periods. But the state on creation of such a trust does not lose power to devise new and reasonable directions to the trustee to meet new conditions arising during its administration, such as the depression presented to trusts holding mortgages. Cf. *Home Building & Loan Association v. Blaisdell*, 290 U. S. 398. Nothing in the Federal Constitution would warrant us in holding that judicial rules tentatively put forward and leaving much to discretion will deprive the legislature of power to make further reasonable rules which in its opinion will expedite and make more equitable the distribution of millions of dollars of property locked in testamentary trusts, even if they do affect the values of various interests and expectancies under the trust. The Fourteenth Amendment does not invalidate the Act in question.

*Affirmed.*

Mr. Justice DOUGLAS, with whom Mr. Justice BLACK concurs.

The New York Court of Appeals stated that in formulating the statutory rule in question the state legislature did no more "than direct a trustee to do what under the decisions of this court he has discretionary power to do." 289 N. Y. 423, 430. And it went on to say, "Before the enactment of this statute, the life tenant could not have demanded as of right the payment to him during liquidation of more of the surplus income than he will receive under the statute. Neither does it appear that the remaindermen could properly have insisted that the trustee should be surcharged if in the exercise of his discretion he had paid to the life tenant the amount which the statute now directs." *Id.* That is a question of New York law on which the New York court has the final say. It is none of our business—whether we deem that interpretation to be reasonable or unreasonable, sound or erroneous. *Sauer v. New York*, 206 U. S. 536, 545-548. And there is no suggestion here that state law has been manipulated in evasion of a federal constitutional right. *Fox River Paper Co. v. Railroad Commission*, 274 U. S. 651, 657; *Broad River Power Co. v. South Carolina*, 281 U. S. 537, 540. Consequently I can see no possible claim to substantiality of any federal question, whatever view may be taken of the due process clause. I would therefore dismiss the appeal.